FEBRUARY 1952 2/6

THE BANKER

VOL. XCVIII No. 313

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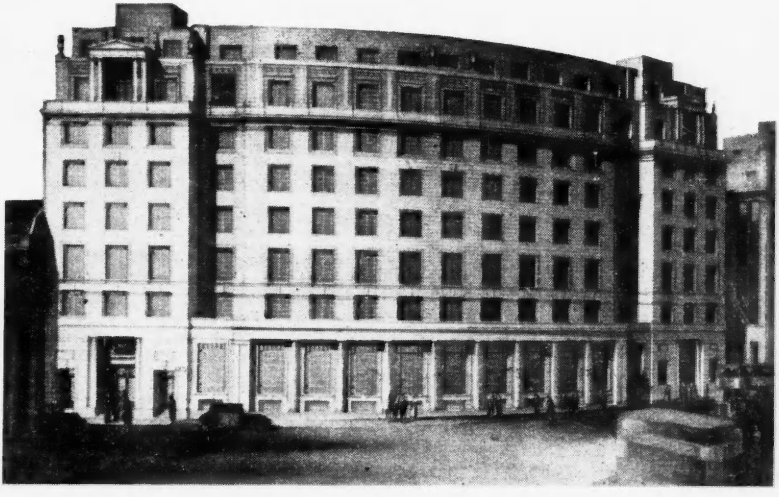

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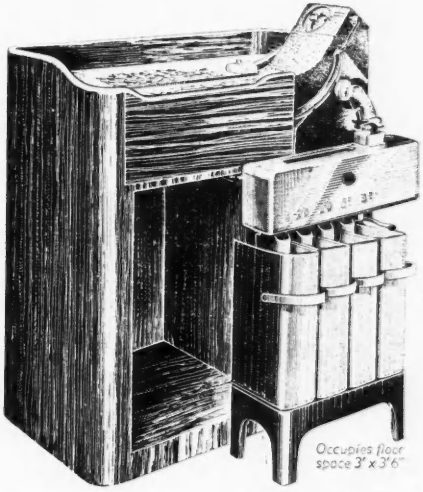

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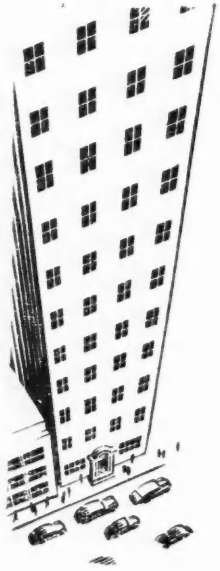

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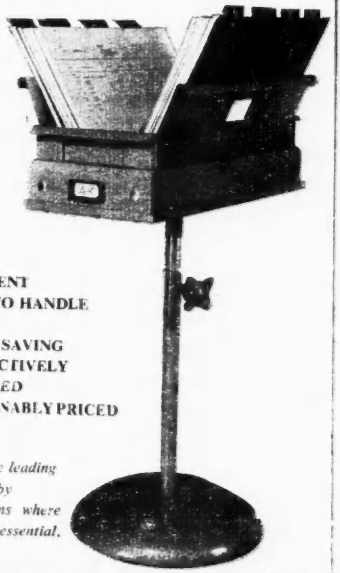

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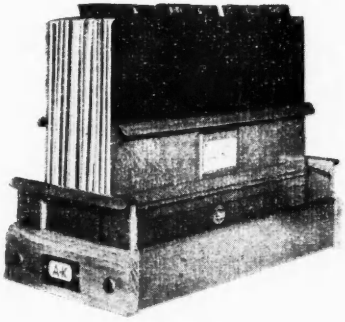

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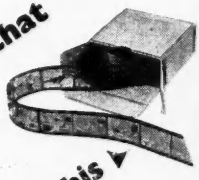

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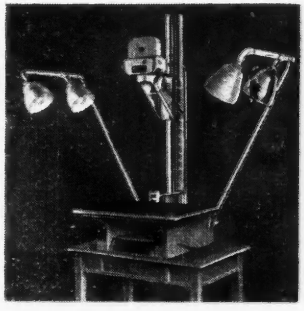

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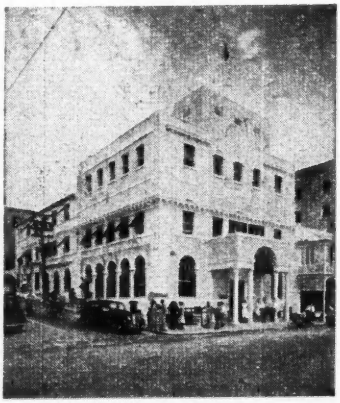

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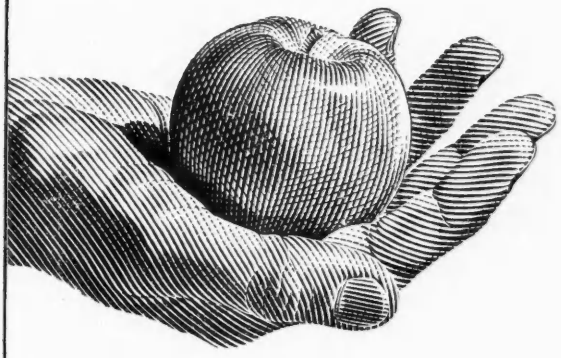

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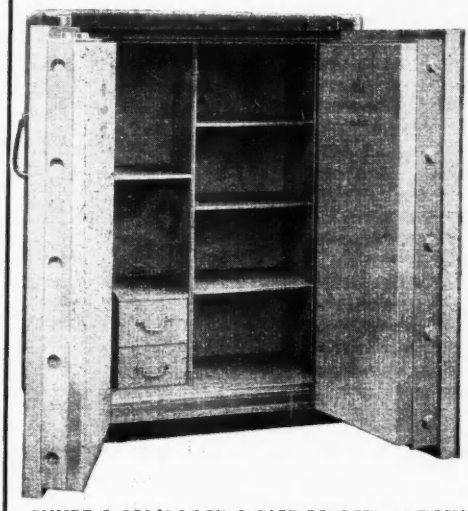

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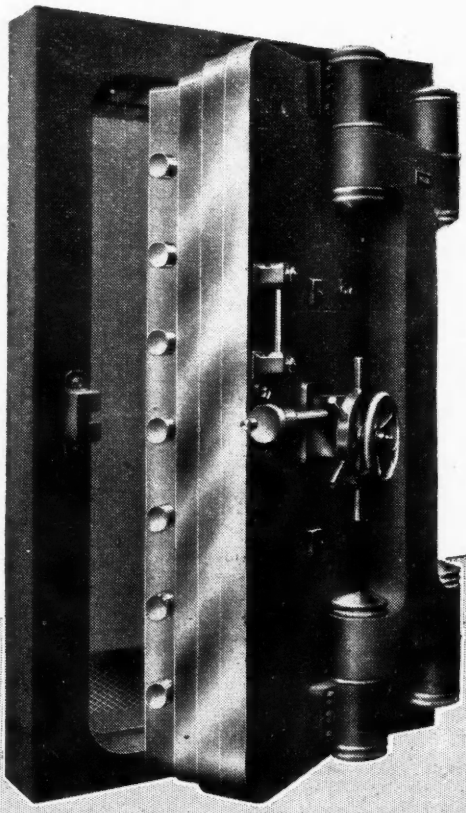

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THE BANKER

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SIR KENNETH O. PEPPIATT, K.B.E., M.C.

(An Executive Director of the Bank of England)

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SIR GEORGE L. F. BOLTON, K.C.M.G.

(An Executive Director of the Bank of England)

A Banker's Diary

Sterling in Distress

In the last three months of 1951 the sterling area's gold and dollar reserves ran down by $934 millions—or by only $74 millions less than in the whole of the three worst years of post-war deficits, 1947 to 1949. In October, as Mr. Butler had revealed in his first speech as Chancellor, the drain was at a peak monthly rate of $320 millions; even in November and December, however, the deficit was still running at some $220 millions a month, or rather more than in the third quarter—before allowing for the $176 millions payment on the United States and Canadian credits, made on December 31. If the end-year rate of deficit continued, therefore—which, of course, it cannot be allowed to do—the whole remaining $2,335 millions in the central reserve of gold and dollars would be gone by the autumn of 1952.

It is impossible to say how much of the responsibility for this plunge into grave crisis should be laid at the door of the United Kingdom itself. The United Kingdom's own dollar expenditure, which normally reaches its peak in the third quarter, last year ran on at a high level right up to the end of December; some of this expenditure had its counterpart in the stockpiling of strategic materials, but some of it was clearly due to the excessive level of domestic consumption. This point will have to be rammed home to the public by the import cuts, and still more by the Government's general measures for disinflation—measures that Mr. Butler may, and certainly should, have notably stiffened in his " retrenchment " speech due to be made while this issue of THE BANKER was in the press.

But, as in 1949, the countries of the overseas sterling area have contributed grievously to the strain. The turn-round here has indeed been dramatic. In the first half of 1951, it will be remembered, the sterling area's sterling balances ran up by £368 millions, of which approximately £98 millions seems to have been due to a capital outflow from the United Kingdom and the rest mostly due to a surplus on current account. In the second half of 1951, however, the sterling area's balances actually ran down, and the indications are that all countries in the group—except Ceylon, South Africa and possibly Pakistan—relapsed into current account deficit.

Part of the overseas sterling area's troubles in the past few months has been due to the sharp reduction in United States purchases of tin, rubber and other commodities; President Truman, in a rather surprisingly optimistic reference to the prospects for sterling area recovery, said last month that this reduction was showing signs of being reversed, and the Churchill-Truman agreement on steel, tin and aluminium provides some grounds for the same hope. But even if American purchases do assume more regularity in the future —indeed even if the promise of such regularity could be written into some sort of long-term contract—it would be most unwise to pitch the target for sterling area solvency on the assumption that American purchases will always run at the level suitable for a time of super-boom. Quite clearly the overseas sterling area must cut its coat according to a more restricted ration of cloth. This does not mean merely that the overseas sterling area must cut its imports from the dollar area—imports that apparently continued to rise in the fourth

quarter of 1951, as in the previous quarter. It means that each country in the area, Britain included, must put its internal house in such order that it will keep its external accounts in balance with the rest of the world as a whole. The " rest of the world ", in this context, naturally includes the E.P.U. countries, to which the sterling area lost $98 millions of gold in the last quarter of 1951; even this figure is struck net of the $39.2 millions reimbursement of gold received from E.C.A. under its guarantee to return to Britain any gold lost through drafts by E.P.U. debtor members on sterling balances accumulated before the middle of 1950.

The Family Confers

It was to meet this urgent need for retrenchment by the sterling rea that the Commonwealth Finance Ministers met in London last month. At this conference a definite plan of campaign was adopted, designed to ensure that " the sterling area as a whole will be in balance with the rest of the world in respect of the second half of 1952 ". The details of this campaign vary from country to country, and none of them has yet been made public; each Finance Minister has taken home a brief-case bulging with proposals to lay before his Government. Inevitably, import cuts form part of the programmes —and may, indeed, form the most tangible part for some time to come. The Finance Ministers' statement, however, rightly condemns undue reliance on such " negative and restrictive methods ", and emphasizes that disinflation in each country that is living beyond its means must be the main road home. Later, Mr. Butler instanced tighter credit policies and some cuts in Government expenditure as the sort of remedies needed. The Finance Ministers also declared that " in some cases long-term borrowing outside the sterling area may be practicable ". This presumably heralds another approach to the World Bank—and possibly to the American or Swiss private capital markets —by such countries as Australia, South Africa and India.

The Finance Ministers have also looked forward further than this. In the first place, an examination is " to be made as quickly as possible of the opportunities for an early increase in the productive power of member countries and of the possibilities of matching available financial and technical resources with the enterprises most likely to achieve that purpose ". Hitherto, most of the individual countries in the group have tried to regulate their own internal investment programmes but there has been little or no attempt at a co-ordinated approach. Although judgment must clearly be reserved until it is seen how the relevant priorities are decided upon, and still more how they are to be enforced, these could obviously be an important step in the right direction.

Finally, the Finance Ministers emphasized that it was their " definite objective to make sterling convertible and keep it so ". An examination is now being set afoot to find out what progressive steps should be taken along this road. Clearly it is crying for the moon to expect convertibility until the central reserves have increased substantially above their present level, but any time spent now in peering beyond the mists will represent valuable time saved when and if fine weather returns. These various " examinations ", especially that concerned with the co-ordination of investment programmes, will clearly involve even closer co-operation on economic matters between the London representatives of Commonwealth Governments. Apart from this,

however—and contrary to earlier forecasts—no steps have been announced for formalizing the administrative machinery for sterling area co-operation.

The American Colossus

WHEN President Truman sent his annual economic message to Congress last month, and accompanied it as usual with the report of his Council of Economic Advisers, he felt able to sing a song of immense industrial expansion, past and prospective. America's gross national product, which was increasing at a rate of about 10 per cent. per annum in the nine months after Korea, has remained remarkably stable since April, at an annual rate of rather under $330 billions. The President believes, however, that it will increase to an annual rate of some $350 billions in 1952. The whole of this increase will be needed for defence, expenditure on which is scheduled to rise from $45 billions now to $65 billions by the end of the year. With business expenditure on plant and equipment expected to be reduced somewhat below its present high rate (which is some 15 to 20 per cent. above pre-Korean levels), the resources left free to be devoted to the manufacture of consumer goods should be little changed from last year. In this there is some cushion for an increase in consumer demand; last year many newly-produced consumer goods went into stock—on a scale that businesses would not be willing to repeat in 1952. It is obvious, however, that there will not be a sufficient cushion to absorb any serious worsening of inflationary pressure if consumers should spend any large part of the new incomes that are expected to be generated by the rise in production. It is for this reason that the President has asked Congress for the $5 billions of new taxes that were trimmed from his request for tax increases last year; even if he gets them—which is most unlikely with an election ahead—Government expenditures of $85.4 billions in the year from next June are expected to exceed Government revenues by $9.4 billions.

It is now a trite saying that nobody should underestimate America's ability to expand production. The planned increases in raw material production and in the basic sinews of her economy—steel production is scheduled to rise by some 15 per cent. by 1954 and electric power capacity by 40 per cent.—are likely to be pushed forward to fruition with traditional efficiency. But it would also be unwise to overestimate the extent to which this bucking bronco can be kept under control by Washington's growing army of economic advisers and stabilization authorities. America was saved from very serious inflation in 1951 only by the unexpected increase of personal saving from about 3 to about 10 per cent. of disposable income in the course of the year. Even with the drying up of demand for consumers' durable goods, inflation had some evil consequences in 1951; the lag in production—and especially in defence production—since last April has been at least partly due to the fact that workers have been kept waiting around on their factory floors for components and tools that the complex system of physical controls has not been able to divert from the civilian market. It is only if these bottlenecks are opened out in 1952 that President Truman's forecasts of increases in industrial production will come true. And over the hill, of course, lies the question of what would have happened if last year's fall in retail sales—which looked suspiciously like a cyclical recession in consumer demand for durable goods—had not come at a time when such slack as it created was swallowed up by rearmament.

THE attempt of the Building Societies' Association to protect borrowers on mortgage from the repercussions of Mr. Butler's new monetary policy appears to be developing into a rearguard action. Two days after the increase in Bank rate to 2½ per cent., the Association issued a " policy statement ". This recorded that attention had been drawn to statements in the Press foreshadowing an increase in the rate of interest payable on mortgage advances, and that the council of the Association had " decided to recommend no change in the rate of interest charged on these advances by building societies ". Although the council had " obviously [to] be guided by future trends, it is and always has been the Association's endeavour to make home-ownership available at the least possible cost ". While the Association may propose, however, it is the individual societies that do the disposing. For some months past, several of the smaller societies had departed from the common pattern of a 2¼ per cent. (tax paid) rate on shares and a 4 per cent. charge on mortgages and were paying and charging 2½ per cent. and 4½ per cent. respectively. Their numbers were augmented about the time of the B.S.A. statement by some of the medium-sized provincial societies, although generally speaking the first step was merely an increase to 2½ per cent. in the rate paid in share departments. The first really serious breach in the united front that the B.S.A. was evidently anxious to maintain came when the Temperance Permanent Society, which had already raised its rates for new mortgages to 4½ per cent., announced that that rate would also apply to old loans and, at the same time, raised its interest rate on shares to 2½ per cent. The Temperance Permanent was followed by the Scottish Amicable, which is to charge 4½ per cent. to all borrowers (both old and new) and to pay 2½ per cent. on its shares. Then came the decision of the Westbourne Park Society to raise its share rate to 2½ per cent., and to charge 4½ per cent. on new mortgages. And finally the Co-operative Permanent has decided to charge 4½ per cent. for new advances.

Building Societies' Changing Rates

All four of these societies are members of the Association. The Co-operative is the third largest in the movement, with assets at the end of 1950 of £63.6 millions, and the other three societies come within the fifteen largest units of the movement. Their break, in greater or less degree, with the rate structure of the past is too serious to be ignored. The building society movement has been extraordinarily successful in recent months in securing new funds, partly, one suspects, because falling stock markets highlight the comforting lack of capital depreciation in building society investments, but also simply because savings as a whole have been resilient as the result of the decline in personal spending. But it is a highly competitive movement and it is most unlikely that the decisions of three leading societies and quite a number of well-established provincial units to pay 2½ per cent. on shares can be without effect on subscriptions to the share departments of societies that have hitherto resisted change. Since the societies must keep a watchful eye on their reserve positions —the falls in the gilt-edged market in 1951 will have reinforced the need for this—any general increase in the rates paid to investors in the movement must, virtually automatically, be followed by a rise in the rate charged on mortgage advances.

Ground has been yielded unwillingly within the movement for three reasons. First, there is a fairly sharp distinction between the experience of some of the

northern, and notably the Yorkshire, societies and the metropolitan and southern societies, with the northern societies benefiting from the native characteristics of their members. Secondly, even those societies in the south whose members lack the phlegm that is typical of the northern investor have been anxious to avoid changes that might not prove reasonably lasting; there is an understandable aversion to "chopping and changing about". Finally, the general implications of Mr. Butler's policy appear to have left some leaders of the building society world unmoved. The banks may have made the second revision of their loan rates deliberately to discourage borrowers. The building societies will charge more because they have to, not because they want to. If their attitude fits oddly into the general monetary picture since November 7, it is no odder than that of the Government that seeks to restrain investment and yet gives housing a high priority. It appears, however, that discussion on the motives of building societies to-day is academic. Forces have now been unleashed that can hardly fail to change virtually the whole interest rate structure of the movement.

More Exchange Freedom

IMPORTANT extensions have been made during the past month in the new-found sphere of freedom within which the London foreign exchange market can operate. In the first place, the market has been allowed to engage in bilateral arbitrage with all European centres in their respective currencies—the sole exception at this moment being Holland and the Dutch guilder. Until this concession was given the two dollars were the only currencies in which London banks were allowed to deal with foreign centres—and, of course, only with the American account area. In all other currencies the buying and selling within the new limits of freedom afforded to the banks had to be done with authorized banks in the London market or, if necessary, with the Bank of England. One by one, the last-comer being the Belgian franc, the European currencies were brought within the realm of bilateral arbitrage dealings. It follows that, except in the case of the Dutch guilder, the previous artificial disparities between rates quoted for foreign currencies in London and in the foreign centres concerned have disappeared. The quotations in London for French, Belgian, Swiss francs and the like are now kept in as close relation with the quotations for sterling in Paris, Brussels, Zurich, etc., as the constant intervention of arbitrage dealing will ensure. This freedom applies to both spot and forward dealings except in the case of the three Scandinavian currencies, where, for the time being, it relates to spot transactions only. It is still impossible to engage in triangular arbitrage in currencies other than the United States and Canadian dollars for the reason that these are the only currencies that are at present free from all exchange control.

The second important concession that has been made to the London foreign exchange market has been the revision and, in nearly all cases, a substantial expansion of the limits given to authorized banks in respect of the foreign exchange positions they may hold. The "position" limits, representing the amount by which the banks can be short or long of foreign currencies in the course of their normal day-to-day spot transactions, have been generally increased. Some expansion has also been granted to a number of firms in the amount of spot currencies they may hold as cover for forward transactions.

The new experiment in freedom in the London foreign exchange market is still yielding an abundant return by way of expansion in the volume of business transacted. The main business is still in the two dollars where the tendency continues to be decidedly "one-way". The U.S. dollar rate in London has hovered at or very close to the Bank of England's official selling rate of $2.78 and in recent weeks the Bank of England has intervened persistently in the market, sometimes in its own name, sometimes through the clearing banks; whatever the form of the intervention, the identity of the seller has always been quite apparent to the market. There has been no official peg in Canadian dollars, which towards the end of January appreciated to parity with the United States dollar.

The New Monetary Policy

THE BANKER is continuing its policy of fully recording and appraising the development of the new monetary system, but in the past month the changes have not been such as to require any extended account of the kind given in each of the two preceding issues.* The focus of interest has shifted to the effects upon the banks themselves and to the light upon the operation of the new measures that can be found in the chairmen's annual statements—matters that accordingly provide the themes of our first two articles this month. The further steps towards exchange freedom are recorded in the preceding Note, while some of the technical implications of the new system are discussed in an article on page 83. In the money market, the principal events have been the relapse of the Treasury bill average rate, from its pre-Christmas peak of just over 1 per cent., to only 18s. 11.05d. per cent. by January 18, and its prompt return to the vicinity of 1 per cent. in the following week—after the market had been forced into the Bank on three successive days, and for larger amounts than formerly.

Meanwhile, readers will have observed that since the changes began we have been devoting our frontispieces to portraits of the architects of the new monetary structure. In our December and January issues we presented the two policy-makers—the Chancellor himself and the Governor of the Bank. Now we present the two Executive Directors most closely concerned at the Bank. Sir Kenneth Peppiatt's distinguished career there extends over forty years. He became Principal of the Discount Office in 1928, a key position that he held both in the last years of the old orthodoxy and the early years of cheap money. In 1934 he was appointed Chief Cashier; in this capacity, especially during the war and early post-war years, he brought a wealth of experience to bear upon the problems of Government finance and the need for new techniques of market control. He became an Executive Director three years ago. Sir George Bolton, after wide experience in merchant banking and foreign exchange, joined the Bank shortly after the inception of the Exchange Account in 1932 to assist in its management. He has since played a leading part in the long series of international negotiations on exchange and currency matters and in the framing and administration of exchange control. He became the U.K. Executive Director of the International Monetary Fund in 1946 and was appointed Executive Director of the Bank of England two years later.

* In response to many requests, the two principal articles—"Re-discovering Lombard Street" and "Bank Liquidity and the Markets"—have been reprinted in the form of a 28-page pamphlet, which will be available within a few days. A few copies of the complete December issue are also still available.

The Bankers Expect . . . .

THE bank chairmen's annual statements mark the end of one of the most eventful, and the beginning of one of the most crucial, years in British banking history. They must therefore be regarded as filling more than their usual rôle of mirrors of City thinking. As each address has appeared, it has been eagerly scanned for an insider's impressions about what is going to happen, as well as for an outsider's views on what the Government ought to do in its economic policies as a whole.

At first sight, it might seem that the bankers have not gone far towards satisfying this new curiosity. Their statements are cast in their usual broad terms. Most of the chairmen express general approval of the move towards orthodox monetary policy, confirm previous analyses of its technical effects on their own portfolios, and then go on to discuss it as one factor among many in their assessment of needed cures for the nation's ills. But to read the speeches in this way is to misunderstand their significance. The vital question, to which an answer must be read between the lines, is whether the monetary policy that the bankers, with their inside knowledge, now see coming into action, is the really firm policy that more and more people are coming to regard as indispensable. Nobody looked for grim warnings from the bankers about loans that were going to be called in, traders that were going to be forced to liquidate stocks at a loss, and inflation that was going to be turned into deflation. The dividing line between intimations of a weak monetary policy and expectations of a strong one was, perhaps, whether the bankers would feel able to cast their warnings to customers in the platitude of the conventional dentist (" This isn't really going to hurt ") or would feel constrained to cast it in that of the sorrowful parent (" This will hurt me more than it hurts you "). The hope was that they would have to use something like the latter approach.

In the event, their approach has lain somewhere in between. The chairmen do, of course, make it clear—even, it may be hoped, to those left-wing politicians who begat what Lord Balfour of Burleigh, chairman of Lloyds Bank, frankly calls the " lie " to the contrary—that the new policy is not one over which they can rejoice in the belief that it will bring lavish financial benefits to the banks. Figures set out by Lord Selborne, the new chairman of the National Provincial Bank, demonstrate once again that the rise in short money rates, net of the rise in deposit rates, will over a full year yield the banks only a tiny sum by contrast with the fall already caused in their inner reserves by the depreciation of gilt-edged values. This point is also made in detail by Lord Linlithgow of the Midland Bank (in a statement that had, through unhappy circumstance, to be circulated posthumously), and by Mr. Anthony Tuke, in his maiden speech as chairman of Barclays Bank.

Most of the bankers also face up to the fact that some businesses—and some workers—will be hurt if disinflation becomes effective. Lord Balfour of Burleigh points out that one of the principal objects of disinflationary policy, as the very means of preserving the purchasing power of the pound and rectifying the fundamental weakness of the balance of payments, must be " to effect as painlessly as may be the transfer of labour to essential industries ".

" Under inflation ", he says, " every industry, however questionable its contribution to the national well-being, is able to earn abnormally large paper profits. Employers in even the least essential industries are thus able to offer good wages and anxious to hang on to their workpeople, even if trade is temporarily slack, while the employees in their turn have no incentive to give up their secure billets to seek more essential work, possibly more arduous, less conveniently near to their homes ". Lord Linlithgow also stresses this immobility of labour in conditions of overfull employment, and sees " further evidence of strain in a reversion in some trades to lengthening delivery dates and renewed difficulty in accepting orders for export markets ". The implication is plain, that paper profits, overfull employment and order books will have to be reduced. The same judgment, that easy-going living and working standards have to be cut, is made in almost identical language by Lord Aldenham of the Westminster Bank and Sir Thomas Barlow of the District Bank (" We have persistently failed to adjust the country's internal economy to the limits of what it can afford "), by Mr. A. H. Bibby of Martins Bank (" It is only possible to spend £1 once ") and Sir Walrond Sinclair of Williams Deacon's Bank (" The 1951 crisis . . . arises from trying to do too much with the resources at our disposal "). Mr. Tuke of Barclays Bank describes this disequilibrium caused by over-stimulation of demand with a vividness and candour that reveal him as a most enlivening as well as shrewd contributor to the annual symposium of bankers' views. In his view, the late Government plied its patient " with successive doses of alcohol when he was already slightly intoxicated. Realizing, however, that he could not be allowed out and about in that condition, they called in the planners to set up an elaborate system of controls with which to check, thwart and generally infuriate the unfortunate victim. And then they gave him another glass of champagne ".

Mr. Tuke's allegory brings out a third point on which there is general agreement among the bankers. This is their welcome emphasis that demand should be cut down by monetary restraints rather than by physical controls. Two of the outstanding dicta in this year's symposium appear in this context. First, Lord Balfour of Burleigh makes the point that monetary restraints are more democratic than physical controls: " When the cut in spending comes from the fact that each of us, individually, is forced to economize, the decisions are taken by the person who in each case is most closely affected and has most knowledge of the relevant facts, including his own circumstances and preferences. The classification of objects of expenditure into ' essentials ' and ' inessentials ' may be convenient administratively, but it is none the less purely arbitrary; beyond a certain point these are question begging terms ". Secondly, Mr. Tuke makes the point that physical controls are inefficient. " I have no belief in the efficacy of any central control of all the manifold wants of fifty million people by means of a mass of permits, coupons and licences, no longer considered merely as necessary evils to be tolerated in time of war and other grave crisis . . . but as weapons with which to repress the anti-social tendencies of those who are so eccentric as to wish to spend their own money in their own way. For my part, I am convinced that in these matters it is better for authority to limit itself to avoiding the creation of conditions in which it pays a man to break the law ".

The bankers might do well to frame these two wise statements, and hang them in their own parlours. For they form an excellent bridge between the

contemplation of general principles and the posing of two harsh specific questions that the banking world should now be asking of itself. The first is: Do the bankers recognize that any disinflationary policy must lead to the reduction of many advances that they had previously regarded as essential? Lord Balfour's limit—the point beyond which "essential" and "inessential" become question begging terms—is long since past. The second question is: Would the banks welcome it if the Government did reduce liquidity sufficiently to force upon them, and off the shoulders of the Treasury directive, a greater share of the responsibility for deciding which of these "essential" loans to cut out? No doubt it would be undesirable to take all the onus off the Treasury directive in present circumstances; this directive, like the mass of controls in the rest of the economy to which Mr. Tuke referred, is "a necessary evil to be tolerated in time of war or grave emergency". But it would be a serious misfortune if the full employment economy were to become one in which the banks always tended to have a margin of unsatisfied but potentially profitable loans, and in which bankers came to lean more and more on directives in deciding which of these to take up and which to refuse. Such an undemocratic development would not only beget a perpetual bias towards an inadequate disinflationary policy; it would also destroy the now reawakened hope that, when the immediate crisis has been surmounted, the automatic monetary regulators of the economy will be sufficiently restored to keep it stable without undue resort to physical controls.

To judge from several of the addresses, the first real test of how far credit restraint is to be allowed to pinch the economy may soon have to be faced in the North of England. As Sir Walrond Sinclair points out in his address to the shareholders of Williams Deacon's Bank, the end of 1951 "saw a falling off in demand" sufficient to give rise to the belief that "the day of easy profits, particularly in the export trades, may well be over". This has especially affected the cotton trade, where, to quote Sir Walrond, "both yarn and cloth output have reached new high levels for the post-war period. Some of this has had to go into stock, a process which cannot go on for long". One of the reasons for this fall in sales, of course, is that the cotton industry has lost some of its competitive power in export markets; a tightening of credit, by making liquidation of stocks inevitable, would be one corrective for this. It is against this background that a passage in Sir Thomas Barlow's address at the annual meeting of the District Bank in Manchester may be noted. Sir Thomas agrees that disinflation is needed but argues that if monetary measures and taxation are pushed far enough to cause "an undue restriction of domestic consumption, there is less solid ground for believing such action would be beneficial either to the country or to essential industries"; he maintains that a substantial offtake by the home market is the only way in which production costs can be kept low, and therefore urges that "it will be necessary to act judiciously in the re-orientation of our industrial output".

There is an inevitable tendency for tough pleas for disinflation and for the restoration of competitive efficiency to melt into something milder at the first sight of distress—sometimes for reasons that might be tenable when seen from any distance, sometimes for reasons that seem good only to those on the spot. The lesson that should be drawn from this is that if Government policy leaves a large buffer zone of marginal advances that are to be attacked only by lending directives and not by pressure on the banks' resources, then, with

the best will in the world, that zone may be penetrated only up to—not beyond—the point where penetration begins to hurt.

How far do the bank chairmen expect that credit will be restricted in the near future, and how much of that restriction do they expect to be caused by pressure on their liquidity rather than by the Treasury directives? To find such answers as they give to this vital question, it is necessary to quote from the speeches at more than usual length:

Mr. Tuke (Barclays): "We are within sight of the time when liquidity may once again be a serious factor in the conduct of our day-to-day business. . . . After so many years in which the climate was almost continually favourable to those who were inclined to carry stocks on borrowed money, whether of raw materials, manufactured goods or securities, the direction of the wind has now changed. I do not suggest that it has settled permanently in the East, nor would it be at all desirable that it should do so."

Sir Thomas Barlow (District): "In what we are called upon to do no drastic deflation is contemplated. On the contrary, we are to exert an influence in support of a gradual disinflationary policy. It is, of course, impossible to know exactly how tight banking restraint upon lendings will have to be. That will be effectively determined by the Treasury through its control over the cash and liquid resources made available to the banks—the credit base itself". Sir Thomas thought it more than likely, however, that in the coming year the bank would be called upon by borrowers "for further assistance, especially from those engaged in all the ramifications of the rearmament programme".

Lord Balfour of Burleigh (Lloyds): "Our money market assets . . . have been brought very near to the level which the banks have regarded in the past as the minimum needed to reinforce the cash reserves. This is . . . a move towards the restoration of the pre-war situation in which a rise in advances would normally be offset by a compensating change in the investment portfolio". In another passage, however, Lord Balfour argued that "even now that the restrictions on lending have been intensified, it will be surprising if the total of advances does not continue to expand for a few months". He also believed that "shrinkage in demand for their products, rather than curtailment of bank credit, is likely to be the main reason for any contraction in the unessential industries in the months ahead".

Mr. Bibby (Martins): "There may have to be some re-orientation of trade, but it is not proposed that there should be disorganization of trade by the sudden withdrawal of banking facilities; it must be recognized, however, that everyone will have to reduce their credit requirements to the minimum and not embark on inessential expansion. The home consumption trades will suffer most and no doubt the hire purchase business, which runs from Rolls Royce cars to electric kettles, will be among these".

Lord Linlithgow (Midland): "For the immediate future it is to be expected that the banks will find it more difficult than in the past to meet even . . . necessary demands. For one thing . . . it is no longer safe to assume that additions will be made to the cash basis to support any legiti-

mate expansion of the volume of bank lending. Thus the more exacting severity called for by the . . . Treasury . . . may be reinforced by quantitative limitation of the banks' lending power. Now that the liquidity ratio has returned to a figure close to the conventional minimum, the scope for enlargement of advances . . . has been abruptly narrowed. Taking all these factors together, the banks have been put into a position in which they may have to restrain severely any further strong upward trend in advances". Lord Linlithgow pointed out, however, that the bank's position still remained very liquid and pointed out that a large part of the new funding stocks will mature this year.

Lord Selborne (*National Provincial*): " The effects of tightening up bank credit may be expected gradually to filter through all sectors of the private economy and make it necessary for individuals as well as companies to consider carefully how their affairs can be arranged without recourse to borrowing. The resources of the banks will be limited ".

Lord Aldenham (*Westminster*): " By this means [the funding], the Treasury has brought about a severe curtailment in the capacity of the banks to make further advances, and I am afraid that many would-be borrowers will find that it will be even harder for them to obtain from us financial assistance which they may well consider to be merited ".

Sir Walrond Sinclair (*Williams Deacon's Bank*): " It is certainly not pleasant to restrict credit and to make it more expensive, as the Government wish, but in this the banks are carrying out official policy in the interests of the whole community". After referring to the funding, Sir Walrond pointed out " It is, however, obvious the banks themselves, after a shrinkage of liquidity of these dimensions, are bound, quite apart from Treasury directives, to tend to cease to be willing lenders ".

These statements of policy, it will be noted, are all very cautiously worded. Taken together, they confirm that the orthodox pressures are already reinforcing the restraint exerted by directives, but they certainly do not suggest these pressures are developing strongly enough to exert any decisive effect. If this is a fair deduction from the statements, it is one that does not seem to be yet worrying the bankers themselves. Presumably they feel that judgment should be deferred. Like all other competent observers, they realize that monetary measures cannot in any case grapple alone with the task of restoring Britain's solvency; every statement emphasizes the fundamental importance of a determined effort to secure effective retrenchment in public expenditure. The first reliable indication of the degree of toughness Mr. Butler will bring to bear in this sphere should be given in the speech expected as this issue of THE BANKER goes to press; but it will probably not be until after his budget speech that it will be possible to gauge how much of the whole task must be performed by monetary policy. Perhaps it is right, therefore, to defer judgment about its adequacy. But unless orthodox measures—as distinct from mere financial directives from Whitehall—provide in the end a monetary policy strong enough to take an increasing proportion of the weight now being thrown upon the physical controls, there will be little chance of the expansion of production and rising efficiency that alone offer a hopeful road towards national equilibrium.

The Banks and Their Reserves

IN one way only has the big banking event of the past year, the change in monetary policy, exerted any major effect upon the bank results reflected in the accounts presented during the past month. The changes in rates and the funding operation, though they will perceptibly increase both the gross yield from assets and the cost of deposits during 1952, occurred too late in 1951 to have much effect upon the current earnings for the year as a whole. But these changes, through their psychological impact on the gilt-edged market, had an immediate and large repercussion upon the market worth of the banks' investment portfolios. The problem of investment depreciation has thus become so dominant in the minds of bankers (not to mention bank shareholders) that it seems desirable, in this survey of the year's banking results and of wider monetary trends, to reverse the customary sequence and to discuss the banks' domestic experience before considering the wider trends that determined it.

The move towards monetary orthodoxy, as everyone is now painfully aware, piled a new and larger depreciation of gilt-edged on to the not inconsiderable fall that had occurred already. Over the year as a whole, although prices closed somewhat above the worst, the longest-dated stocks showed declines of fully 18 per cent., a figure also shown by " Daltons " though not by Consols. In general, stocks with a longer maximum life than ten years at the year-end showed losses of 9 to 14 per cent. (though it should be noted that most of these stocks have in fact a maximum life of at least fifteen years). The fall in the shortest stocks (three years or shorter) was 2 per cent. or less. So violent a movement had not unnaturally given rise to widespread fears that the banks might be unable to provide out of their inner reserves the whole amount required to write down their portfolios to market value. It was known that these reserves had been severely depleted by the gilt-edged slump of 1949; and it also seemed likely that the new monetary policy and expected budgetary policy, which clearly increase the risk of bad debts, would make the banks feel obliged to earmark further inner reserves against this contingency. In the circumstances, there seemed a possibility that some of them would follow the precedent of 1931, when nearly all the big banks met the depreciation of investments partly by transferring substantial sums from published reserves.

In fact, none of the big banks has done so.* The strain upon them is discernible in their published accounts only from the fact that all of them, after maintaining their customary dividends, have returned the whole of their undistributed profits to inner reserves under the head of " contingencies "—and most of them (notably Barclays) have augmented these transfers by running down the profit balance carried forward. For the " Big Seven " banks, the aggregate sum transferred to contingencies is £4½ millions, compared with less than £2 millions in 1950 and just over £3 millions in 1949. This, of course, is only a fraction of the total investment depreciation actually sustained. The aggregate investments of the clearing banks stood at £1,555 millions before the funding operation, so that—as several bankers have pointed out—an

* The Provincial Bank of Ireland, however, took £300,000 from its reserve fund, reducing it to £340,000.

average fall of no more than 1 per cent. would have represented fully £15 millions. Since the banks do not disclose the distribution of their portfolios (though several banks have this year given a broad indication of their position) it is impossible to make any confident guess at the average fall actually experienced. It is most unlikely, however, to have approached 5 per cent. in any bank; at the other extreme, it would have required a very cautious policy, pursued over a lengthy period, to have kept it below 3 per cent. The aggregate book loss, as Lloyds' chairman pointed out, must have run into " tens of millions ".

TABLE I
PROFITS AND APPROPRIATIONS
(£ 000's)

	Net Profits		Dividends			Contingencies Premises and Pensions		Reserve Fund and Carry Forward	
			Rate %	Net Cost					
	1950	1951	1950-51	1950	1951	1950	1951	1950	1951
Barclays	1972	1908	14	1146	1094	Nil	1000	826	– 185
Lloyds	1762	1816	12	988	943	250	900	523	– 27
Midland	1987	1925	16	1334	1273	650	650	3	2
Nat. Provincial ..	1455	1470	15	782	747	Nil	750	673	– 27
Westminster ..	1471	1405	18	855	816	600	600	16	– 10
Martins	733	725	15	343	340	375	375	15	11
District	513	508	18½	286	273	50	225	178	11
W. Deacon's ..	260	259	12½	129	123	150	125	– 19	10

In the light of these estimates, the fact that the banks have avoided drafts on published reserves appears as a tribute both to strength of the position that had been built up internally and to the increasing caution observed in investment policies. It seems evident that the lessons of 1947 and 1949 have been well learnt, and that the banks have been losing no opportunity to shorten the average life of their portfolios. Several of the banks have stated that after the writing down their investment reserves still show a surplus; but it is evident that, speaking generally, the inner resources have sustained another heavy inroad and cannot now be as adequate as the banks must wish as they

TABLE II
" BIG FIVE " PROFIT COMPARISONS

	1947	1948	1949	1950	1951	Change in 1951
	£	£	£	£	£	%
Barclays ..	1,637,706	1,879,943	1,866,279	1,971,834	1,908,437	– 3.2
Lloyds	1,635,612	1,674,329	1,709,276	1,761,603	1,815,858	+ 3.1
Midland	2,002,570	2,025,728	2,006,414	1,987,320	1,925,316	– 3.1
Nat. Provincial ..	1,347,929	1,383,387	1,413,120	1,454,811	1,469,765	+ 1.0
Westminster ..	1,391,076	1,431,532	1,460,557	1,471,031	1,405,453	– 4.5
	8,014,893	8,394,919	8,455,652	8,646,599	8,524,829	– 1.4

look towards the risks of 1952 and beyond. Any determined effort to combat inflation is bound to produce some business casualties; it may provoke a further fall in gilt-edged; and it may, in any case, force the banks to convert a portion of their " book " depreciation into realized losses.

Meanwhile, an important factor in the ability of the banks to absorb the past year's depreciation has been the strength of their current earnings. There is little doubt that the amounts provided for contingency or investment reserves *before* striking the published profits figures have been larger than they were a year ago—despite the mounting tempo of rising costs. Gross earnings from

assets have certainly expanded further, and probably more substantially than they did in 1950. The banks have again been employing a larger volume of resources; as Table III shows, the average level of deposits rose by 2.4 per cent. A larger proportion of total resources, moreover, went into the most remunerative types of asset. The average level of advances rose by 14 per cent., compared with the rise of 11.3 per cent. experienced in 1950, and the average ratio of advances to total deposits rose from 26.7 to 29.6 per cent. Investments, too, were on the year's average substantially higher; but roughly half this movement was attributable to the funding operation which, although it will provide more income than would have been secured from the surrendered Treasury bills, has not contributed anything to 1951 profits.

It should be noted, too, that the trend of interest rates was rising even before the change in monetary policy. In an effort to safeguard their revenue against the pressure of rapidly mounting costs—it is certain that a much heavier burden of salaries and pensions lies ahead, apart from the bigger additions made during the past year—the banks last summer agreed with the discount market upon a substantial increase in rates for commercial bills and the relevant call money, and shortly afterwards launched their revision of

TABLE III

CLEARING BANK AGGREGATE FIGURES

(£ millions)

	At December 31			Average of Months		
	1938	1950	1951	1938	1950	1951
Deposits	2253.0	6368.2	6332.6	2277	6015	6162
"Net" Deposits *	2188.0	6100.0	6035.3	2217	5811	5931
Cash	243.4	540.1	530.7	241	497	511
Money Market Assets	409.8	2000.6	1569.3	431	1848	1797
Call Money	150.5	592.2	597.7	151	550	569
Bills	250.3	1408.4	971.6	280	1298	1228
Treasury Deposit Receipts	—	455.5	101.5	—	430	247
Investments plus Advances	1601.3	3171.7	3896.4	1613	3108	3446
Investments	635.0	1527.7	1965.5	637	1505	1624
Advances	966.3	1644.1	1931.0	976	1603	1822

* After deducting items in course of collection.

charges for advances. These changes, though effective for only part of the year, must have had a perceptible effect upon gross earnings. On the other hand, the Treasury's further switch from Treasury deposit receipts to bills will have slightly reduced the aggregate return from these two groups of assets.

Finally, the growth in income from commissions has probably been no less significant than that in direct interest earnings. Foreign business, trustee business, and the provision of miscellaneous services have all been expanding, and in some instances the charges have been raised. Most public comment on bank earnings probably tends to underrate, too, the revenue from commissions charged for the general conduct of accounts. Many of these have been raised during the past year; and those that are assessed as a percentage on turnover will, of course, have produced an increased revenue in any case, in consequence of the rise in the general monetary turnover.

The year's profit experience, therefore, has been a blend of three ingredients —heavy investment depreciation, good gross earnings and steeply rising costs. Policy in the striking of published profits has also had to take account of the big rise in costs that lies ahead, the growing risk of bad debts, and the importance of replenishing inner reserves. The actual figures, set out in Table II,

do not tell any more of the year's story than is customary. The changes shown are tiny; and the only worthwhile comment is that the decline shown in the aggregate figure is appreciably less than the equivalent of the additional 6d. that has had to be borne in income tax.

Deposits and the External Deficit

Although the average level of deposits during the year was higher, the net change between the two balance-sheet dates was very small. Except for 1949 (when net deposits rose by only £51 millions), the past year is the only one since before the war in which the volume of money has been approximately stabilized. The net fall of £65 millions in deposits contrasts with a rise of £136 millions in 1950. This contrast, which at first glance may seem favourable, is, however, no more than a reflection of the rapidly mounting strain upon the national economy—the strain that forced the external balance of payments from its 1950 surplus of £229 millions into a deficit of twice that amount. This violent swing from large lending abroad to heavy borrowings and drafts on reserves has greatly reduced the Government's need for bank finance—

Table IV

CLEARING BANKS: Changes in Annual Periods

(£ millions)

	1944	1945	1946	1947	1948	1949	1950	1951
Deposits	+ 513	+ 305	+ 836	+ 249	+ 265	+ 2	+ 166	− 36
"Net" Deposits ..	*+ 519**	*+ 291*	*+ 779*	*+ 243*	*+ 231*	*+ 51*	*+ 136*	*− 65*
Cash	+ 78	+ 36	− 37	+ 2	—	+ 30	+ 9	− 9
Money Mkt. Assets ..	*+ 62*	*+ 276*	*+ 421*	*+ 231*	*− 47*	*+ 454*	*+ 321*	*− 431*
Call Money ..	+ 48	+ 54	+ 180	+ 48	+ 6	+ 86	+ 21	+ 6
Bills	+ 14	+ 223	+ 241	+ 183	− 52	+ 368	+ 299	− 437
T.D.R.s	+ 360	− 144	+ 36	− 272	+ 109	− 604	− 338	− 354
Invests. and Advances ..	*+ 22*	*+ 130*	*+ 359*	*+ 281*	*+ 168*	*+ 179*	*+ 137*	*+ 725*
Investments ..	+ 11	+ 69	+ 193	+ 56	− 5	+ 34	+ 16	+ 438
Advances	+ 11	+ 61	+ 166	+ 225	+ 172	+ 145	+ 121	+ 287

* Peak of war-time credit expansion.

despite the deterioration in its domestic cash position in consequence of the increased expenditure on armaments. This large supply of finance from external sources, taken in conjunction with the lag in the defence programme, explains why the Government was able to make large net repayments of indebtedness to the banking system, whereas earlier in the year it had been expected that it would be a net borrower.

The year's stability of deposits has, in fact, been the resultant of two major but opposite forces that have chanced to have approximately equal weight. The first of these forces was the greatly increased net repayments by the Government (which, on the customary basis of estimation, appear to have amounted to well over £350 millions, compared with only £30 millions or so in 1950). The second was the greatly increased rate of growth in advances. These expanded during the year by no less than £287 millions, or by 17.4 per cent. This is the biggest annual movement ever recorded; it compares with a growth of £121 millions in 1950 and far surpassed the previous peak of £225 millions, touched in 1947. The major reasons for this rapid acceleration are now familiar: the steadily mounting pressure upon the working capital

of industry that had become apparent in earlier years, and the fact that the new issue market was quite unable to provide an adequate relief for bank finance by funding operations, would have raised advances substantially even if the year had not been marked by the dramatic rise in primary commodity prices and the associated all-round rise in domestic costs.

In addition, the nationalized public utilities have continued to be very heavy borrowers from the banks. Despite the funding operation begun by the Gas Council by its loan flotation of last July, bank loans to the utility group at the latest date for which the quarterly classification is available (it is shown on page 114) totalled £94 millions, in contrast with £42 millions twelve months previously. The continued pressure from these public borrowers raises some pointed questions now that the banks have more compelling reasons than formerly for keeping a tight hold on their total advances. The purposes for which this finance is required are of a kind that ought to be financed through the long-term market, and the banks should not be expected to provide more than is strictly needed as a " bridge-over ". The gaps between funding operations are presumably dictated by the Government's desire to time the issues

TABLE V

THE DECLINE IN BANK LIQUIDITY

	Liquid Assets * %			Advances and Investments * %		
	October	November	December	October	November	December
Barclays	40.0	32.8	33.8	54.1	63.1	61.0
Coutts	35.3	30.6	32.0	63.9	69.1	66.7
District	38.0	30.5	30.4	56.1	65.5	64.3
Glyn Mills ..	30.6	30.7	40.6	65.4	66.2	55.4
Lloyds	40.0	32.8	32.8	54.6	63.2	61.3
Martins	39.8	33.2	34.5	54.6	62.3	60.6
Midland	40.2	32.8	34.1	54.4	62.0	60.7
National	23.4	23.6	26.5	80.4	79.4	77.9
Nat. Provincial ..	39.4	30.6	33.7	55.9	66.0	61.1
Westminster ..	36.7	30.4	30.8	57.4	65.0	63.3
W. Deacon's ..	37.3	32.8	34.9	56.4	62.8	57.7
Aggregate ..	**39.0**	**32.0**	**33.2**	**55.7**	**64.0**	**61.5**

* Ratios are calculated on gross deposits.

to avoid undue shock to the gilt-edged market, and the fact that this bank finance is obtainable on privileged terms presumably encourages a ready acceptance by the nationalized boards of the wishes of the monetary authorities. But if these tactics now contribute to strain upon the banks' liquidity ratios, ought the banks to be expected to take a loss by selling investments simply because the nationalized boards are waiting for a less unwilling market ?

As usual, a high proportion of the rise in total advances occurred during the first half of the year. In this period the expansion amounted to no less than £238 millions, fully £100 millions more than in the similar period of 1950. But, whereas in the second half of that year funding operations actually produced a slight fall in the outstanding total, in this past half-year there was a further net rise of £49 millions. Even so, the contrast between the advances pressure in the first and second halves of the year was much more marked than in 1950. The resultant influence on the behaviour of deposits during the year was much more than offset, however, by the swing in the other major influence —the Government's need for bank finance.

This need, of course, is also strongly subject to seasonal factors. The effect

of big revenue surpluses in the final quarter of the Government's fiscal year regularly ensures a substantial net repayment of Government indebtedness to the banks during the first half of the banking year, while revenue deficits usually necessitate borrowings from the banks during the second half. During the first half of 1951, when the seasonal factor was reinforced by the re-emergence of a deficit on the external balance of payments (the deficit then was £122 millions, compared with a surplus of £42 millions in the first half of 1950), net repayments to the banks amounted to some £440 millions, or some £100 millions more than the comparable 1950 estimate. Thus, despite the much steeper rise in advances, there was still a substantial net fall in deposits.

During the second half-year, as the external balance of payments plunged much more rapidly into deficit, the relief to the Government's domestic cash position grew correspondingly. Government borrowings from the banking system during the half-year appear to have been well under £100 millions, in contrast with an estimated £350 millions or more in the second half of

TABLE VI
CLEARING BANK LIABILITIES
(£ millions)

	Deposits *						Acceptances, Etc.	
At Dec. 31	1938†	1949	1950	1951	*Change in 1951* %	*Increase since 1938* %	1950	1951
Barclays	429.3	1254.4	1272.2	1269.5	−0.2	196	64.6	64.2
Lloyds	391.9	1130.9	1147.7	1169.6	+1.9	198	96.2	104.5
Midland	408.3	1321.0	1304.0	1321.5	−3.2	182	78.1	89.2
Nat. Provincial ..	305.3	776.5	838.3	816.8	−2.6	167	38.2	39.5
Westminster ..	348.4	807.7	815.1	806.3	−1.1	131	51.5	77.9
Martins	99.1	305.1	303.2	314.4	+3.7	217	29.9	23.3
District	82.1	231.3	239.7	238.6	−0.5	191	13.0	13.2
W. Deacon's ..	37.5	118.9	130.8	139.5	+6.6	272	8.7	11.9
Glyn Mills	32.4	77.0	77.2	77.1	−0.1	138	10.1	7.6
Coutts	23.0	50.7	48.8	48.2	−1.2	109	2.4	2.0
National	30.7	71.8	72.4	75.0	+4.4	106	1.2	1.2

* Excluding balances from subsidiaries and excluding profit carried forward.
† Weekly averages for December.

1950. The half-year's rise in deposits, at £116 millions, was therefore less than one-third of the steep rise that occurred in the second half of 1950.

The great force of this external factor, which during the year as a whole has eased the pressure on the volume of money to the extent of perhaps £500 millions (this is Mr. Churchill's estimate of the year's external deficit), and which in the previous year was exerting an opposite influence to the extent of £250 millions or more, gives some measure of the monetary strain that will have to be resisted as and when the import cuts and other physical measures reduce the external deficit to manageable proportions. Unless the budgetary and financial measures, including monetary pressures of the requisite intensity, are kept closely in step with the hoped-for improvement in the balance of payments, the recent stability of deposits will inevitably give place to another large expansion, and the balance of payments improvement itself will not endure.

The part that the banks now expect orthodox monetary policy to play in this vital process is discussed in the preceding article in this issue, in the light of the chairmen's statements. It is still uncertain whether the orthodox pressures will be pushed very far; and most of the bankers, though naturally drawing attention to the reduction in their liquidity ratios, are at pains to

emphasize their adequacy by comparison with pre-war standards. The actual figures are set out in Table V, from which it will be seen that there is indeed, at this seasonal peak, a small margin in hand if 30 per cent. is considered the datum line. Although the level will fall automatically in the next few months of revenue surpluses (probably less sharply, however, than most public comment seems to have supposed), it is not to be expected that the banks will show much concern at any change that could be regarded as merely seasonal.

TABLE VII
MAIN EARNING ASSETS
(£ millions)

	Investments*				Advances †			
At Dec. 31	1938‡	1950	1951	*Change in 1951* %	1938‡	1950	1951	*Change in 1951* %
Barclays	98.4	310.9	415.2	+ 33.6	197.6	323.7	363.3	+ 12.2
Lloyds	109.0	273.7	360.2	+ 31.6	163.5	288.8	341.7	+ 18.3
Midland	122.0	301.2	422.5	+ 40.2	207.4	344.3	393.6	+ 14.2
Nat. Provincial ..	84.0	150.5	202.4	+ 26.9	139.4	246.0	295.1	+ 20.0
Westminster ..	112.2	209.6	251.2	+ 19.9	133.4	208.9	262.6	+ 25.7
Martins	35.1	74.5	101.2	+ 35.8	43.5	74.8	88.6	+ 15.6
District	20.3	72.0	88.5	+ 22.9	31.1	56.4	64.7	+ 14.7
W. Deacon's ..	11.6	37.3	42.2	+ 13.1	14.4	31.1	36.9	+ 18.6
Glyn Mills	10.7	24.2	20.4	− 15.7	9.6	15.8	20.6	+ 30.4
Coutts	7.6	10.3	18.1	− 6.2	9.3	12.8	14.0	+ 9.4
National	14.2	32.8	29.8	− 9.1	17.1	25.5	29.1	+ 14.4

* Excluding "Trade" investments, etc. † Excluding balances with, or loans to, subsidiaries.
‡ Weekly averages for December.

This probably means that the liquidity weapon will not seem really dangerous unless the ratio fails to show a seasonal recovery in the new fiscal year. But if the balance of payments is to be brought rapidly towards equilibrium, it would require a very tough budget indeed to put the Government in a position

TABLE VIII
OTHER ASSETS
(£ millions)

	Cash Ratio*		Call Money		Discounts		T.D.R.s	
At Dec. 31	1950 %	1951 %	1950	1951	1950	1951	1950	1951
Barclays	8.25	8.38	88.0	89.5	315.6	237.7	97.5	22.0
Lloyds	8.41	7.81	116.1	104.3	236.1	188.9	84.0	18.5
Midland	8.33	8.24	88.4	82.2	390.6	265.3	100.5	20.0
Nat. Provincial ..	8.62	8.95	84.0	107.3	107.1	95.0	50.0	14.5
Westminster ..	9.48	8.68	101.7	82.0	134.1	98.6	60.5	14.5
Martins	8.09	8.40	38.7	47.0	56.3	35.1	22.0	4.0
District	8.27	8.52	17.1	19.6	48.5	32.7	17.0	5.0
W. Deacon's ..	8.54	8.63	18.3	25.0	15.4	11.8	9.5	2.5
Glyn Mills ..	6.95	9.37	20.3	20.8	3.3	3.4	3.5	0.5
Coutts	8.18	7.97	8.8	9.3	1.5	2.4	2.0	Nil
National	7.82	8.66	10.7†	10.7†	0.9	1.0	Nil	Nil

***As officially** computed, i.e. based on deposits as defined for purposes of the *monthly* statements.
† Treasury bills included with call money.

in which it would not need, in the new fiscal year, to borrow substantial sums —which, if raised through the banks, would tend to restore their liquidity ratios. The real strength of the liquidity weapon may therefore depend, in the end, upon the willingness (or reluctance) of the authorities to raise any cash that is needed by direct borrowings on the market—and also to resort to market issues to replace the new serial funding bonds as they fall due.

Forward Exchange Then and Now

By Paul Einzig

ON December 17, 1951, dealings by banks in forward exchanges—as distinct from transactions for account of the Bank of England and at its fixed official rates—were resumed in the London market after a lapse of more than twelve years. Between 1939 and 1951 there was still some activity in forward exchanges in the outside world. Free dealing was maintained in New York and a few other centres, while in some other countries there were black markets in currencies for forward delivery. But even these markets that remained in operation were mostly difficult ones with a narrow turnover. Owing to the exchange restrictions that were in force in most countries there could be little or no arbitrage between them and they were very largely isolated from one another; local discrepancies between supply and demand were therefore apt to produce sharp divergences between the rates quoted at the same time for the same exchanges for the same periods. Because of the narrowness of the markets the rates were very sensitive and relatively small operations were liable to lead to inordinately large swings.

London had no interest in these markets in forward exchanges, except as barometers that showed what foreigners thought of sterling. British banks were not allowed to deal in exchange as principals, either for their own account or for account of their customers; they worked simply as agents of the Exchange Control. Hence, British importers and exporters were unable to make use of the forward facilities offered by overseas markets; they were provided with alternative facilities by the Bank of England at official artificially fixed rates without reference to the factors that determine the forward margins in a free market. Moreover, these same rates were charged to British banks on their own transactions for the covering of the exchange risk on their authorised working balances in foreign currencies. No possibility was left to the banks or their customers of either speculating in the overseas markets or of engaging in arbitrage operations with them.

The sudden reopening of the market for forward dealing therefore found London wholly unprepared, and those concerned had to re-learn the theory and technique of forward exchange in a hurry. Luckily there are many people in London who remember the system as it operated before the war. In the few weeks since the restoration of the market they have been able to brush up their practical knowledge and theoretical background to a sufficient extent to ensure the functioning of the restored market without any major hitches. Pre-war knowledge is not, however, sufficient by itself. The system to-day differs in many respects from the one that was in operation before the war. The object of this article is to draw attention to the main differences and to examine their effects.

There are seven main differences between the rules governing the pre-war and post-war markets. In the first place, only genuine commercial transactions are now permissible. Before the war there was no need for the banks to ask their customers whether a buying or selling order for foreign currencies for forward delivery was linked with some genuine commercial transaction.

Both banks and their customers were entitled to engage in speculation or arbitrage. This freedom has not been restored. Admittedly, the banks are no longer required to apply to the Bank of England in advance about each forward exchange transaction. The authorized dealers can deal in forward exchanges with their customers and among themselves at rates settled by conditions in the market. But at the end of each day they have to submit the relevant "E" Forms containing the details of their transactions with their clients. Because of this subsequent scrutiny of transactions, the Bank of England's control over the character of forward operations is therefore—in principle, at least—as complete as it was before the restoration of the "free" market. The banks are entitled to buy and sell forward exchanges only in instances in which they are satisfied, on the basis of their knowledge of the exchange regulations and the Bank of England's interpretation of them, that the Bank of England would have authorized the purchase or sale of forward exchanges before December 17. In doubtful or borderline cases, or when large amounts are involved, they may even feel impelled to consult the Bank before executing the transaction.

Secondly, only authorized dealers can deal in forward exchanges in the market. As the list of authorized dealers is long this difference is not, perhaps, of fundamental significance (though the exclusion, both from spot and forward dealings, of firms that used to deal before the war does raise an issue of principle), but there are important restrictions on dealing with foreign banks. Thanks to the extensions made last month, British bankers can deal spot or forward with banks in the American account area and all the more important continental countries except Holland, and can deal spot in Scandinavia. In each case, however, these dealings must be confined to the currency (or, in the American area, currencies) of the area concerned. Under the prevailing practice the foreign banks have to sign a declaration that the purchase or sale of forward exchange is based on genuine commercial transactions.

Thirdly, the extent to which banks can maintain *uncovered* forward exchange positions is now limited. No definite limits have been fixed at the time of writing; the authorities want to ascertain the requirements in the light of experience. Before the war open exchange positions had no legal limits, but they were limited by the prudent practice followed by all banks of standing. The customary rule was that the foreign exchange departments were entitled to enter into uncovered positions during the course of each day's dealings, but had to cover these positions before the close of the market.

Much more important, however, is the limitation on the amounts of foreign currencies that banks are entitled to hold with the forward exchange covered. The actual limits, like those of the maximum of uncovered positions, have not, however, yet been definitively fixed. In principle, the main difference here relates to the method of securing cover. Before December 17 the banks were entitled to hold limited working balances in foreign centres, and they covered the exchange risk through the sale of the forward exchange to the Bank of England; now they have to find their own forward counterpart in the market (though they may purchase spot cover from the market or, if unobtainable there, from the Bank of England at its official rate, subject to the general limitation of working balances).

Necessarily, these limitations impose an important restraint upon activities in interest arbitrage. Before the war these activities were subject only to

the limitations imposed by the extent of the banks' available liquid monetary resources, and by the self-imposed rule that no more than a fraction of their assets should ever be thus employed. These limitations were elastic, and the amounts engaged in interest arbitrage through swap operations were liable to increase as and when such operations became attractive because of the emergence of a premium (or narrowing of the discount) on the forward exchange of the receiving centre (e.g. if the discount on the forward dollar narrowed unduly, or if the rate went to a premium, the flow of funds to New York might tend to increase).

Interest arbitrage is now also restricted by the ban on overdrafts on the banks' " nostro " accounts. British banks are not allowed either to grant such overdrafts to overseas banks or to obtain them abroad for the purposes of interest arbitrage. From time to time before the war such overdrafts supplied a substantial proportion of the resources engaged in interest arbitrage operations, though, of course, their rôle was important only when the discrepancies between interest parities and forward rates became wide enough to leave a margin of profit to cover the relatively high overdraft charges.

Before the war it was possible to use the proceeds of fine bank bills for interest arbitrage. This can still be done to a limited extent. There is no ban on acceptance credit facilities, but as these facilities were often misused in the 1930s for the purpose of drawing finance bills, there is now a rule that they can be used only for genuine commercial purposes. By comparison with pre-war experience, a much higher proportion of the bills drawn on the credit lines are now documentary bills—hence, incidentally, the need of foreign branches and acceptance houses to employ much larger staffs. In consequence, the proceeds of these bills cannot be directly employed in interest arbitrage. A similar result can, however, be produced indirectly. If the discount on forward sterling widens sufficiently, it becomes profitable to make full use of acceptance credit facilities all the time. In given circumstances the profit on the swap (the yield obtained by buying foreign exchange spot and reselling it forward at a premium) plus the interest obtained on the funds while employed in the foreign centre may exceed the discount rate and the commission paid on the acceptance credit, so that the borrower then actually collects what may be regarded as a " negative interest " on the amount borrowed.

Finally, arbitrage in space, which played an important part before the war, is now handicapped by the rule under which only genuinely commercial transactions are permissible, and also by the continued ban on " triangular " dealings (except where the two overseas centres concerned are both within the American account area, notably, of course, New York and Montreal) and the ban on dealing with Scandinavia forward and with Holland, whether spot or forward. Nevertheless, the fact that " bilateral " dealings within these limits make it possible to cover commercial transactions in the centre where the forward rate is more favourable should go a long way towards reducing discrepancies even in the absence of triangular arbitrage in space. In currencies in which even " bilateral " arbitrage is still forbidden the discrepancies are likely to remain abnormally wide, much wider than before the war.

So much for the rules under which the market operates. What, now, of the effect of these rules on the pattern of operations ? One obvious consequence is that markets in forward exchanges remain much narrower than before the

war. The actual turnover on commercial account is necessarily larger because of the higher prices, but there are no speculative dealings and the turnover on arbitrage account is very small. There are fewer participants in the market than before the war, and it is much more difficult to find a counterpart for big items than in pre-war days. To be able to undo the swap resulting from a large forward transaction with a customer and cover it immediately by a spot transaction, banks have to do several swap transactions of smaller amounts. "Marrying" transactions for the same dates have become very difficult. A fresh complication, unconnected with the narrowing of the market, is the increase of the practice of transacting forward exchanges for delivery on optional dates—say, any day up to a month or two months or three months. In prevailing conditions it is difficult to cover these otherwise than by a spot transaction.

Another noticeable feature is that deviations of forward rates from the interest parities are likely to be wider and more lasting than before the war. Even in pre-war days there were some wide discrepancies from time to time, whenever there was basic disequilibrium foreshadowing a change in the value of the spot rate, or whenever there was a persistent speculative pressure upon a particular currency. On many occasions the funds that banks were able and willing to employ in interest arbitrage were not sufficient to counteract the speculative pressure on the forward rate, especially as the authorities in the country whose currency was under pressure generally took steps to make money conditions tight. These practical limitations on the funds available for arbitrage before the war, however, were as nothing compared to the official limitations on their availability now. Since the purchase of spot dollars and their sale for forward delivery secures a high yield (at the time of writing, about 4 per cent. p.a.), and, moreover, short-term rates are higher in New York than in London, there should be a tendency for a high proportion of such liquid funds as are available for the purpose to be held there. Despite the profit on interest arbitrage, however, the extent to which the banks engage in interest arbitrage is relatively small. One reason for this is that various exchange regulations keep the amount of funds that can be held in New York relatively low. Nor can American balances, or such other foreign balances whose transfer is permissible, materially swell the volume of funds engaged in interest arbitrage. For a large part of the sterling balances that could be transferred to New York by their non-resident owners were transferred there last autumn owing to rumours of impending sterling devaluation. The pressure on the forward sterling rate due to the inadequacy of interest arbitrage is somewhat reduced by the fact that certain types of importers are allowed to cover their future dollar requirements by buying spot dollars and keeping them on deposit in New York. This is done in order to avoid increasing the cost of imports on which the margin of profit is narrow by requiring the importers to buy forward dollars at their high premium. It should be noted, here, that while exchange restrictions, in preventing interest arbitrage on an adequate scale, tend to cause and perpetuate abnormal discrepancies, they also tend to prevent large-scale speculative operations in forward exchanges. It is difficult in existing circumstances to work up a sweeping bear campaign or bull campaign in foreign exchanges through forward exchange operations.

Another effect of the official restriction placed on arbitrage is, of course, that any speculation against sterling does not lead to quite such a dangerous

drain on the gold reserve as before the war. In itself speculative pressure on the forward rate does not lead to a loss of gold either under the gold standard or under an inconvertible currency the spot rate of which is kept stable by official support. It is only as and when the widening of the discount on the forward exchange leads to the transfer of funds for the purposes of interest arbitrage that loss of gold arises. In theory, at any rate, such an outflow of funds for interest arbitrage is now impossible—though there are, of course, other ways in which anticipation of a fall in the spot rate adversely affects the gold reserve, independently of the forward market.

One cost of insulating the gold reserve by placing restrictions on interest arbitrage is that these restrictions tend to cause a widening of the discount on forward sterling. The effects of this should be noted, for they are largely similar to those of a depreciation of the spot rate. A widening of the discount causes an increase in the sterling price of imports—except in the case of importers who are allowed to cover their requirements through the purchase of spot exchanges instead of forward exchanges—and also an increase in the sterling proceeds of exports, or alternatively a reduction in their prices in terms of foreign currencies. In other words, an artificial depreciation of forward sterling changes the terms of trade against this country in the same way as a devaluation of spot sterling would. The extent of the change is likely to remain relatively moderate, because even a forward discount of, say, 4 per cent. per annum represents an addition of no more than 1 per cent. to the cost of imports for which payment is made within three months.

At the moment, although forward sterling is at a heavy discount against the dollar, it stands at an abnormal premium in relation to the French franc. British importers of French goods stand to benefit by the premium inasmuch as it reduces the cost of the imported goods—unless they prefer to leave the exchange uncovered in the hope that by the time payment is due the franc may be devalued. (This is done, of course, also by many American and other importers of British goods, which accounts partly for the wide discount on forward sterling in relation to the dollar and other hard currencies.) On the other hand, British exports to France are to some slight degree handicapped by the additional expense incurred by French importers through having to cover their sterling exchange risk at a premium. Should the tide turn and should it become once more fashionable to anticipate a revaluation of sterling rather than a devaluation, the terms of trade would change slightly in favour of this country through the development of a premium on forward sterling in relation to the dollar and other currencies. But, since there are no exchange restrictions in operation to limit the transfer of funds from New York to London to take advantage of a profit on interest arbitrage, the premium on sterling in relation to the dollar is not liable to widen to anything like the same extent as the discount.

Taking everything into consideration, it seems that, so long as exchange restrictions continue, it is idle to expect the resumption of operations in forward exchanges to exert their natural effects of producing healthy conditions in the exchange markets and of promoting a more fundamental equilibrium by helping to enforce monetary discipline wherever that is needed. From this point of view, it seems unlikely that the discrimination between commercial and speculative operations will disappear for many years to come, at least so far as sterling is concerned.

Inflation in France

By Charles Janson

NO European country has experienced a more violent rise of prices since Korea than France. According to the *Institut National de la Statistique* the French cost of living rose from 100 (January-June, 1950) to 124 in August-September, 1951. During the same period the West German index climbed to 108, the United States index to 111, the Italian and the British to 113. As the report of the Finance Committee of the National Assembly observes: " These figures seem to show that, quite apart from the general rise in the price of raw materials which has affected all countries, France has exhibited a special sensitivity to internal inflationary pressures ".

It will be seen from the accompanying table that the general rise of prices in France has continued in spite of a steady fall in the price of imported goods after April, 1951. In part this has been due to the usual lag between a change in the price of imported raw materials and in the price of retail goods. But the principal cause has been the increase of labour costs; this increase has been accentuated by the 15 per cent. rise in the minimum legal wage in September, for any increase in the minimum legal wage tends soon to be followed by a roughly equivalent rise of all wages. Partly because of this wage inflation, there have been sharp increases in agricultural prices and in the prices of those basic materials that are subject to Governmental decree (especially coal, electricity and gas). At the same time there has been a considerable speculation in stocks; part of this speculation, which has inevitably driven up prices, has been due to a flight from the currency.

In mid-October M. René Mayer started a new drive against inflation by restrictive monetary measures. He raised the discount rate of the Bank of France from $2\frac{1}{2}$ to 3 per cent. and its rate for advances against securities from $3\frac{1}{4}$ to 4 per cent. In addition, the *Conseil National du Credit* tightened the incredibly tight controls that the Bank of France exerts over credit conditions. These controls, and this process of tightening, were described in THE BANKER last month.* The main steps were the introduction of new—and more strictly enforced—rediscount ceilings for the commercial banks, an instruction that the banks should achieve the required ratio between Government securities and deposits on a daily basis instead of once a month, and a decision that borrowing on commercial bills should be included among the forms of borrowing that were subject to the Bank of France's " prior authorization " procedure. At the same time, the Bank of France decided in future to devote its energies to the sifting of the applications for large credits only (500 million francs and over) and to leave the smaller fry to sifting by the commercial banks themselves.

Three weeks later, in November, the Bank of France again raised its discount rate, to 4 per cent., and its rate for advances against securities to $4\frac{1}{2}$ per cent. Simultaneously, the rates on Government bills with three months or less to run and on monthly loans against Government acceptances were put up from 3 to $3\frac{1}{2}$ per cent. This second jump in discount rates was considered inevitable in Parisian financial circles, for right up to the end of October

* See " France's Experiment in Credit Control " by J. S. G. Wilson

the volume of credit had continued to expand, and the Bank of France's holding of Government bills and commercial paper had steadily grown, while foreign exchange drained away. The demand for foreign exchange by importers for genuine trading purposes was on the increase during September and October; in the latter month the adverse balance of payments exceeded $150 millions *vis-à-vis* E.P.U. countries alone. To the legitimate demand for foreign exchange was added a large speculative holding of foreign currencies caused by fears of a devaluation of the franc. Meanwhile, businesses were turning more and more to the banks for liquid capital while they clung to stocks.

Although it is too early to make a considered judgment, there is evidence that the new measures are already exerting some effect. The new credit ceilings have been very strictly enforced by the Bank of France and the commercial banks have co-operated with the economic policy of the central bank in the granting of facilities to customers, including those loans that are no longer subject to the old form of prior authorization. The Governor of the Bank of France believes, however, that certain industries are still being given too much credit; there are excessive stocks of timber, sugar, flour and tinned food, of leather, rubber, shoes and textiles. At the end of the year, the banks were therefore "invited" to be even more rigorous in withdrawing credit

WHOLESALE PRICES IN FRANCE. (100 — 1949)

	1950			1951										
	May	June	Dec.	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sep.	Oct.	Nov.
General Index	104.2	103.4	120.4	123.0	130.0	134.0	140.2	140.7	137.6	134.7	133.9	137.5	146.1	150.5
Foodstuffs	102.7	97.4	109.1	106.6	110.0	112.7	116.0	121.0	117.3	114.8	117.2	124.5	130.7	132.5
Fuel and power	103.0	104.3	111.5	115.0	116.5	118.9	126.8	123.7	121.6	123.2	122.1	132.5	139.6	140.9
Industrial goods	106.0	108.3	133.6	140.5	152.5	158.0	166.3	163.9	161.2	156.3	152.7	150.6	161.9	169.7
Imported goods	119.8	124.2	170.0	178.5	200.7	206.0	210.0	192.5	185.3	172.8	167.2	162.2	162.8	169.0

from speculators and to divert credit to those industries, large and small, where an increase in productivity and exports is essential. The Bank of France seems to be in a position to put some bite behind its bark. After nearly three months' operation of the new regulations the rate of increase of the note issue, previously about 25 per cent. per annum, has fallen considerably. In addition, from November to December the rate of increase in wholesale prices decelerated to 0.5 per cent., against 5 per cent. from September to October. With an improved balance of payments, M. Mayer can claim the appearance of having scored at least a limited success.

It is generally agreed that the only permanent solution of France's economic problem lies in a large increase in production. France, like other O.E.E.C. countries, is committed to try to increase production by 5 per cent. per annum during the next five years. On the face of it, this target is quite attainable; in the year after Korea French production rose from 124 (June, 1950) to 143 (June, 1951). Higher production in the future should be one of the fruits of the very large recent investments in the coal-mines and electricity. But there are serious bottlenecks. The country is still very short of coal and its manufacturing industries are technically backward. There is a shortage of skilled labour, especially in the building industry; this shortage was hampering

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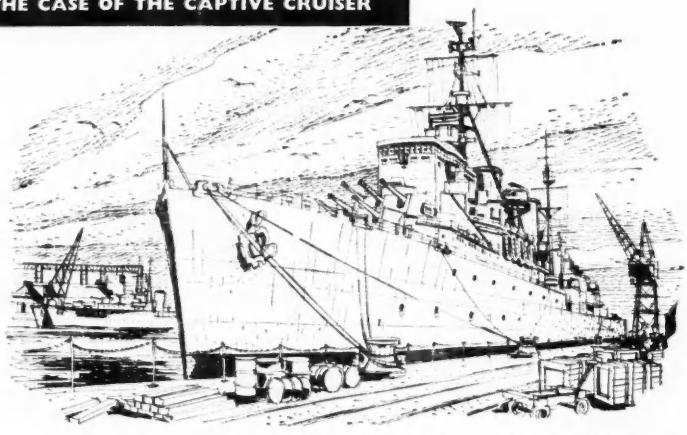

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alleviation of the housing shortage—France's greatest single social problem—even before the recent worsening of the shortages of steel and cement. Scarcity of materials and of labour at home are aggravated by a tenacious protectionism and by the restrictive action of trade associations; in the last few years, therefore, there have been determined efforts to channel investment into the basic industries, which are genuinely trying to expand production. An increase in agricultural production by 10 per cent. over the 1934-38 average has already been achieved, but only at the cost of a rapid increase in prices; there is at present no prospect that France will become a food-exporting country on a large scale—which would be one way out of her long-term problem.

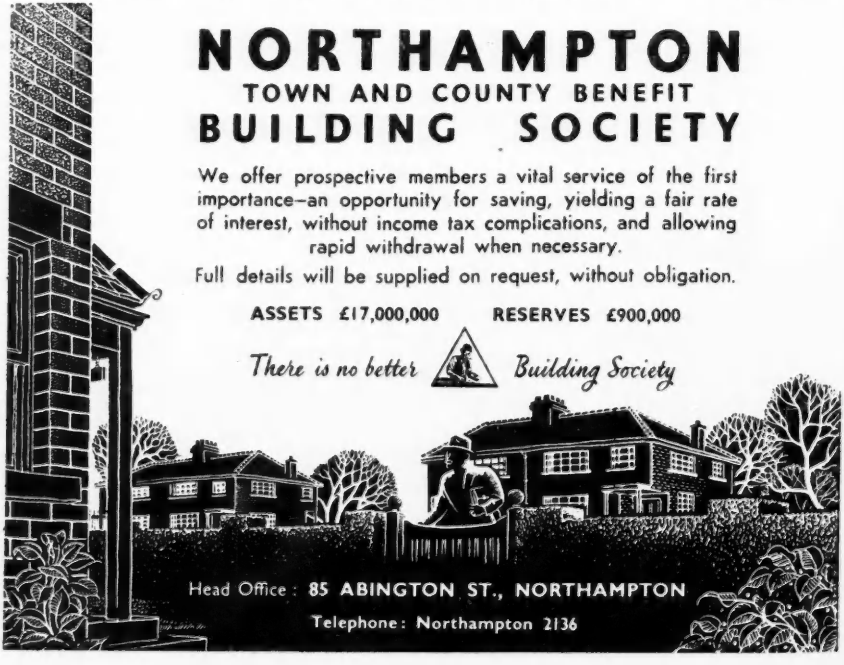
All this suggests that any increase in French production in the next five years will be insufficient to remove inflationary pressure—unless spending is cut. One of the greatest spenders is the State. The salient feature of French budgets of the last few years has been the very high proportion of Government expenditure that has been devoted to investment and military items. In 1952 61 per cent. of expenditure went to reconstruction, investment and the defence effort. In a budget that itself amounts to nearly 35 per cent. of the national income, this expenditure is clearly extremely inflationary—the more so because in many instances the equipment of factories has been insufficiently co-ordinated, with the result that production itself is unnecessarily delayed. Mistakes of this kind are partly responsible for the drag in rearmament production during 1951.

Perhaps the most deadly feature of the French economy, however, is the virtual disappearance of private saving; as in so many other countries private saving has now sunk to about 5 per cent. of incomes against 14 per cent. in 1939. The middle class of pre-1914, which was one of the foremost saving groups of Europe, has been impoverished to the point of extinction. The wage-earners, who now benefit from social security and pay little heed to the future, spend any surplus over vital needs on wireless sets and household goods. The large new class of *commercants*, which possesses none of the characteristics of the former bourgeoisie, spends more and more of its surplus purchasing power on such things as automobiles and refrigerators. Moreover, any funds that they do save do not find their way on to the capital market; far too much of them are " invested " instead in gold.

The atrophy of the capital market means that the Government has to undertake a large proportion of the country's needed investment expenditure itself; and this, together with the shortage of private savings, means that taxation must be driven up to higher and higher levels. Unfortunately the difficulty of collecting direct taxes in France has caused the system of taxation in vogue to be repressive and inducive of revolt by the wage-earners. At the moment it is divided as to 60 per cent. into indirect taxes, as to 30 per cent. into direct taxes and as to 10 per cent. into customs dues; in the United States—to quote a comparison often made in France—the comparable proportions are 10 per cent. in indirect taxes, 85 per cent. in direct taxes and 5 per cent. in customs dues. Every increase in taxation—such as that of 10 per cent. proposed in the 1952 budget—accentuates the injustice of the system. But every attempt to adjust taxation to encourage savings—such as the provision in the 1952 budget that 5 million francs may henceforth be inherited tax free by a husband or wife or direct descendant—leads to complications on the revenue side.

Since private real investment is so hampered in France by the sad state

of the capital market, it is probably true that France could reach a state of disinflationary balance with its overall budget accounts (both current and capital) making a less impressive picture on paper than Britain's would need to do. As in other continental countries, there is some excuse for the polite fiction that the counterpart funds to United States aid should be treated as a Government receipt—or rather there was some excuse so long as internal savings to an equivalent amount did exist but were going to waste in gold and hoards from which the Government could not borrow. But in an economy that is suffering from every disease at once, and in which inflationary pressure is constantly recurring, the need to make real withdrawals from personal purchasing power keeps on mounting between one Budget day and the next. So far this need has been partly met by the levying of supplementary indirect taxes (on such things as petrol and tobacco) towards the end of the fiscal year. But these supplementary levies are becoming ever more painful and difficult. The Report of the Finance Commission on the Budget contains an eloquent commentary on the dilemma of a state that never quite knows whom to cajole or how to do it: " We want to encourage production by economic means: at the same time we discourage it by taxation. We want to revive saving: at the same time we discourage it by income tax and by estate duty. We proclaim the need for re-equipment of industry and investment: at the same time we hamper it by obsolete laws regarding the valuation of stocks and amortization ". The policy, in short, is one of moving from expedient to expedient, and those who have to carry it out necessarily find each new turn of the screw more unpalatable than the last. This is a recipe for continual political crises, rather than for economic recovery.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What Policy on Resale Price Maintenance?

By John Ryan

The new Government has not yet given any indication of its policy toward resale price maintenance. In the August, 1951, issue of THE BANKER *Mrs. Margaret Hall argued in favour of the Labour Government's proposal to introduce legislation that would ban all resale price fixing by manufacturers. In the following article Mr. John Ryan, after taking issue with Mrs. Hall on a number of points, puts forward his own suggestions on the direction in which a solution to this problem might be found. Mr. Ryan was a member of the Lloyd Jacob Committee, which reported in* 1949 (*Cmd.* 7696) *in favour of permitting resale price maintenance by individual manufacturers but against permitting groups of manufacturers to apply price-fixing sanctions that would not be open to individual firms.*—ED.

IN an article in THE BANKER last August Mrs. Margaret Hall put forward the case for prohibition of resale price maintenance. She agreed with the Labour Government that no manufacturer should be allowed to try to fix in advance the prices at which his goods are sold to the retail customer, whatever the channels of distribution through which those goods passed. Mrs. Hall's arguments do not seem to me to accord with the weight of evidence presented to us at the Lloyd Jacob Committee's enquiry in 1949. At that enquiry we heard evidence from some 90 organizations or individuals, and were thus presumably given a fairly full appreciation of what informed or interested opinion in this country thought or knew about resale price maintenance. The Committee did not, incidentally, publish its full hearings—as Mrs. Hall appeared to suggest it did; all it did publish were agreed summaries by fifteen different trades of their activities in collectively administered schemes.

After hearing the full evidence I find myself in disagreement with Mrs. Hall on a number of issues. Some of these are points of detail. For instance, I do not agree that resale price maintenance started with the marketing of branded goods, nor that it was manufacturers who originally pressed for its adoption. I also consider that Mrs. Hall frequently confuses maintenance of *fixed* resale prices with maintenance of *minimum* resale prices. The Lloyd Jacob Committee was concerned only with the former—and necessarily so, since it is nearly always a "fixed" price that is marked on the package of a branded article. A manufacturer may be anxious to prevent resale of his products below a given price, but it may be just as important to him to prevent the full potential of his market from being restricted by an attempt by a distributor to get higher prices than the market will pay. Again, there seems to be no practical evidence to support Mrs. Hall's assumption that "price maintenance without limitation of entry will produce an excessive expansion of distributive trades", while her conclusion that the only alternative to banning resale price maintenance is to jeopardise the international competitive efficiency of the United Kingdom, and with it the international

position of sterling, surely attributes far more to the practice than can ever be its effect.

The wide public debate on this whole issue of resale price maintenance has unfortunately become bedevilled by political considerations. The conflict of political viewpoints is almost entirely concerned with the measures taken for the enforcement of resale price maintenance rather than with the essential nature of the subject itself. During the period in which resale price maintenance has grown up, an increase in public emphasis on the need for efficiency and economy in production and distribution has proceeded side by side with a rising public recognition of the need to investigate monopolies and restrictive practices; the passage of the Monopolies and Restrictive Practices (Inquiry and Control) Act, 1948, for instance, carried a large measure of agreement amongst the main political parties. Continuation of restrictive practices, or of any inefficient or outmoded system, may, of course, properly be condemned as anti-social because of the corroding effect that feather-bedding has upon initiative. But history shows that this reaction can sometimes go too far. When the Statute of Monopolies was passed in the reign of James I it originally banned all monopolies save those arising from letters patent of invention. In later years, public dislike of monopolies haunted even such useful things as brilliant inventions—the spearheads of industrial development. The Patent Acts now make it impossible to enforce letters patent that are used to procure restrictive practices. Any who are interested should examine Section 57 of the Patent Act, 1949, to see how ingeniously the issues are made the subject of enquiry in the High Court.

One form of permitted statutory monopoly, however, is the registered trade mark; these are at present governed by the Trade Marks Act of 1938. The law has for years recognized the benefit to trade and public of safeguarding trade marks from misuse. My own view is that we could most usefully adopt a similar practice with regard to brand names. All reputable proprietors of registered trade marks would desire to preserve their badges of quality from any stigma. That is why I believe the crux of the objection to the " loss leader " practice, to which I shall refer later, is not so much retailer dissatisfaction as the inevitable " cheapening " of the brand in the eyes of the public.

Economic Changes Caused by Branding

Any discussion of this problem should start with a recognition that resale price maintenance is clearly a development in our distribution system that raises new issues in management both by reason of the age in which we live and the considerable increase in its use in this and other countries; some 30 per cent. of domestic private consumers' expenditure is now believed to go on articles and commodities of which the prices are fixed or recommended by producers. One cannot divorce this discussion from consideration of significant changes in the world economy.

Resale price maintenance is almost always associated with branded goods —that is, goods that are marked in such a way that their original source may be identified. The branding becomes effective when the public is made aware of this distinction—usually through nation-wide advertising undertaken by the producer to bring his article before the public notice, to emphasize advantages between his product and others and create a demand for it. Such

branding may not be a substitution for an unbiased certification of real quality, but it is obvious that there are advantages in it; manufacturers, distributors and consumers alike agree that experience up to date shows that there is little variation in the quality of articles sold under any particular brand except, of course, for abnormal variations such as might be necessary in war-time and, one hopes, are understood as inevitable and temporary. Many of the recent Committees of Inquiries and Working Parties, such as the Boot and Shoe, Cutlery, Furniture, Glassware, Pottery and Agriculture inquiries, have recognized these advantages of branded goods, and the general increase in branding would hardly have gone on as fast and as smoothly as it has done if there had been any serious grounds for keenly felt objection to it. Between the wars branding was extended to bulky and perishable goods—for instance, bread, sugar, butter and even oranges. There is no reason to doubt that this tendency will continue. The development of self-service methods of retailing, of which I shall say more later, and the introduction of frozen foods will inevitably imply a further move towards packing and branding by producers.

This growth of branding has materially affected the conditions of retail and wholesale trading. It has disturbed the incidence of functions traditionally assigned to distributors, and some of these functions have been taken over by manufacturers. There has been a decline in the importance of selective buying by retailers as " advisers " to customers. Customers have become so well acquainted with various brands that in many cases they have made up their minds what to buy before entering the shop. When this happens, the retailer ceases to be the chief interpreter or creator of public taste, and this throws such functions of distribution right back on to the manufacturer. He, more and more, uses his own sales organization, or firms who specialize in this type of work, to assess the type and quantity of goods that are required. He also seeks to influence public requirements by national advertising, reducing thereby some of the traditional technical selling functions of the distributor and turning him more and more into a neutral channel between producer and consumer. For good or ill this has led to greater competition between specialist and general shops. There are now only some 15,000 chemists' shops in this country, but 150,000 others sell pharmaceutical or toilet preparations. There are perhaps 10,000 traders specializing in the sale of tobacco products, but over 400,000 tobacco licences. There are 12,000 specialist confectioners, but over 200,000 shops that sell some chocolate or sugar confectionery. The specialist distributor may call this " dabbling " in the retail trades to the detriment of the established specialist shops; but it happens, and its implications cannot be avoided.

Branding has not had this effect on all branches of retail trade. In the ordinary consumable article the housewife can test a brand that she buys every week and if it does not come up to her expectations she can try another one or an unbranded product. But when one comes to articles that are bought only infrequently, such as a motor car or a radio set or a washing machine, that method of trial and error is not available. The goods are relatively expensive and the cost of a mistake is likely to be serious. The customer does not usually have sufficient technical knowledge himself and therefore he still remains, even with a branded article, dependent on the advice of the distributor. Moreover, for such articles the actual purchase does not end the transaction; regular service and replacement of faulty parts is almost inevitable. Since,

however, the brand can still be identified as the product of a particular manufacturer who depends on the goodwill of the public, the manufacturer has a special interest in ensuring that his goods are sold and serviced only by properly qualified agents.

Reactions to these Changes

The attitudes of manufacturers, distributors and consumers towards resale price maintenance have to be viewed against this changing background. Consider, first, the object of a manufacturer in attempting to fix a price. He offers to the public an article of a certain quality and, in order to take full advantage of the potential demand for it, plans to cater for a particular price range. This is increasingly done as a result of market surveys; it is important, particularly in mass production, that, once a manufacturer has decided the range of price and quality for which he intends to cater, he should not lose possible customers because of the charging of a retail price above that range. It is also essential that he should have a reasonably stable distributive system that he can seek to bring into full use by national advertising. He therefore seeks increasingly to have a stable price so that he can ensure a steady flow of his production as it comes out of the factory.

By and large, he must make use of the distributive system as he finds it. He must secure the support not only of the lowest cost distributors but of the general run of distributors as well. When he introduces a new product, therefore, he has to create conditions whereby distributors as a whole will stock it and continue to stock it. Past experience appears to have shown manufacturers that if a nationally-advertised brand is sold at varying prices in neighbouring shops the demand for it—reflected in the distributors' orders to the manufacturer—decreases substantially; this applies in particular to articles that are bought " on impulse ". But, in publishing prices and making them widely known, the manufacturer sets up a standard by which the extent of price reductions may be easily identified by the public, and therefore creates circumstances whereby retailers may be tempted to use his product as a " loss leader ". (I use the term in the accepted sense of an article sold at a price cut drastically below the established retail price. Such cuts are a form of advertising by the retailer to attract customers into his shop in the hope that they will at the same time purchase articles showing a higher rate of profit; the increase in turnover of articles showing a normal rate of profit can often outweigh the losses sustained on the sales of the leading line.)

A widely known standard price also creates other problems. The public often considers that variations from the recognized price are an indication that quality has deteriorated and their confidence in the product is shaken. Sometimes, indeed, they are right. Where a technical article requires after-sales service and the availability of proper replacement parts, the distributor whose costs (and prices) are low may be in that position because he provides a less efficient service of this kind. The price quoted by this sort of retailer may not be a correct measure of the final cost of the purchase.

What now of the distributors? In face of changing economic conditions it is not unnatural that established wholesale and retail traders should try to preserve stable trading conditions and to maintain their position in the distributive system. In particular, small independent retailers who used to be specialists in their own field and who take great pride in the element of crafts-

manship that they feel they bring as a distributive service, naturally seek to preserve a financial return commensurate with the service that at one time they alone provided. The practice of resale price maintenance has been a most convenient instrument for them for this purpose; here again, it is perhaps the degree of stability in the price structure that they have sought to preserve rather than the actual level of their former profit. Generally speaking, the distributive margins on price maintained goods are rather lower than on other types. There is good reason for this. If the value of the brand is appreciated by the consumer from experience and if large-scale advertisement is bringing the article to his regular notice, then he goes into the shop ready to buy an article and not to have to discuss what he requires, so that both time and "expertise" are reduced at that point in the distributive chain.

The wholesaler also has an interest in a steady fixed price—though not such a marked one. One of his functions is to supply retailers with all their needs with a minimum of delay, and he must exercise a great deal of planning in the level of his stocks. Acute price competition, by disturbing the level of demand, would require the carrying of much greater stocks. The wholesaler also acts as a reservoir for the retailer and to some extent as a buffer against stock losses; price reductions therefore fall with special severity upon him.

To get the view of the consuming public or "the man in the street" is always difficult, but there are indications that consumers, too, feel that fixed retail prices afford certain clear advantages. There is a general acceptance that branded articles carry some guarantee of standard quality. It is a convenience to know in advance what an item will cost, so that household expenditure can be checked and planned. The value of "free service" for a defined period seems to be widely recognized. Where, however, the consumer does feel uncertain is whether the actual prices themselves are altogether fair. What the household shopper normally seeks to secure is value for money; this is possibly the reason, as stated earlier, for suspicion that articles sold below the standard price are in poor condition.

Does the System Increase Prices?

Is there any evidence that the system of branded products and maintained prices increases the cost of living? The manufacturer settles his fixed price for an article by adding his own cost to the distributor's margin. He is able to determine what his cost of production will be up to the point at which the article leaves his own factory; he bases this estimate on the most efficient method of producing the quantity needed to satisfy a given market demand. He can also alter that cost by advertising. What level of advertisement is in the public interest is a matter on which there are bitterly opposed views, but it should be remembered, as has been argued above, that advertising may reduce costs in the field of distribution.

Except for the influence that may be exerted in this way, distribution costs are largely outside the manufacturer's control. They necessarily vary considerably according to the type and size of business carried on, the class of market catered for, and the geographical location of the particular trader or of a given shop. Costs may remain fairly constant over a period of time but they will vary from locality to locality and from shop to shop. Traders may also vary their costs to suit their particular policy. A retailer may

elect to advertise, or to provide extensive delivery, credit or other facilities without extra charge. He may decide to reduce these services to a minimum and to trade on a " cash and carry " basis, or to speed up the time taken to serve customers by engaging more staff.

Unfortunately, statistics on distribution costs are very sparse. Those of us who have had an opportunity to examine the methods whereby traders calculate their mark-ups, however, are in no doubt about the high degree of conventionality that exists. Gross margins for distributors are commonly reckoned not as a sum of money, but as a discount that represents a certain percentage of the final selling price; it is clear that distributors tend to judge the adequacy of the margin allowed to them by the percentage relationship that it bears to the selling price, and do not examine it so much as a cash return for distributing the product concerned.

Despite the variation in distribution costs, it is general for manufacturers practising resale price maintenance to establish a nation-wide standard price. It is perhaps too generally accepted that this is essential, and I suggest that a change might be considered here. Although there are to-day more geographical variations in selling prices than in the 1930s—petrol is a current example—there was at least one outstanding example of geographical variation before the war. This was the London Price Schedule introduced by the better-known proprietary chocolate manufacturers in 1932. This prescribed minimum retail selling prices for the London area that were about 10 per cent. lower than the advertised price for the rest of the country, as a result of a cut of approximately one-third in distributors' margins. The introduction of the special price schedule was not, I think, an acknowledgment that chocolate was used as a " loss leader " in London, but of the fact that, with a densely populated shopping area and a high turnover per shop, costs of distribution were lower in the London area. In the same trade in 1936 different levels of resale prices were established for wholesalers in different parts of the country.

The development of " self-service " may make further steps in this direction advisable in other trades. This form of retailing is said to have led to a marked reduction in the cost of distribution in other parts of the world, particularly in America. What therefore is to happen to a product that is sold in a self-service store as well as in the more general and older type of shop? Is the manufacturer to give a lower margin in a field that he may think it worth while to stimulate? The issue is a live one, and if circumstances make it possible for self-service to move forward faster than hitherto, then it would of course be upon us in a more acute form. We cannot afford to ignore it even at this stage, and I submit it as an aspect of the problem that urgently requires deeper thought.

By and large, the manufacturer of a branded line, secure in the acceptance of his product by the public, may consider himself in a strong position to dictate a lower level of margin to the distributor than that distributor would otherwise get. Manufacturers may therefore seek to break the traditional level—in fact some have done so with appreciable success—but obviously the measure of their strength varies with different products and in different circumstances. The newcomer into a particular field cannot, of course, have such power at the outset; inevitably he must generally gravitate towards the traditional margin. Now there is clear evidence that pre-war margins on

many goods have been maintained substantially at the same percentage level over long periods, irrespective of changes in retail price; hence, for these goods, the cash value of the distributive margin varies with the price of raw material or the cost of manufacture, and does not depend on the cost of retailing itself. The connection between price and cash margin may perhaps be less direct than this statement implies; but the correlation is too close to be merely coincidental. This is one way in which the present system of distribution may be said to be uneconomic.

It is also true that, generally speaking, a customer who wishes to buy his goods on a " cash and carry " basis cannot obtain for himself any reduction over the customer who takes long credit and expects delivery; he thus, in effect, pays for something that he neither has nor wishes to have. How can such a position be resolved, if at all, inside a fixed price basis? The question is not easy to answer, but this is perhaps not as conclusive an argument against resale price maintenance as some people think. Given the present system of distribution, resale price maintenance has diverted competition from price to service. But without resale price maintenance, the system of distribution itself might have been more expensive or less satisfactory—even for the customer who sets little store by service.

Competition in service is an entirely different thing from price-cutting and the use of " loss leaders ". Aggressive weapons of the latter kind may not reflect any actual or expected saving in operating expenses. There is an obvious difference between making a noteworthy reduction in the price of specially selected goods and a gradual reduction in the general level of prices over a whole range. The consumer does not necessarily obtain any lasting benefit from the former; and in fact such action may be harmful to the interests of consumers in general.

In so far as price competition has in the past been the means of creating economical and efficient methods of distribution, it must be allowed freedom of action; in distribution, as in many other fields, old borders are constantly being removed and new technique introduced. There is no reason to suppose there is not still room for improvement, and I doubt if public opinion would accept conditions in which new-comers are not free to enter the field, in which enterprising traders are unable to introduce new methods or in which the lower-cost or more efficient distributors are inhibited from offering the public the advantage of reduced prices or improved methods. Yet, as the proportion of price-maintained goods grows—particularly when it is, as hitherto, tied fairly closely with conventional margins—it undoubtedly creates an extending rigidity in the distribution system.

There is the dilemma. So far it has in general not been solved. In this article, I do not pretend to have even tried to suggest a solution. What I have sought to do is to draw attention from both sides to the relevant problems that are inherent in the practice as it has grown up, and to stimulate thought towards ways and means of solving them. There are many difficult questions to resolve, but I am convinced that the pressure of economic necessity will sooner or later drive us to recast many of our old methods. If we wait until the dam has burst, many things valuable in themselves may be swept away in the rush. Careful investigation now will not only evince a willingness to move with the times, but should produce a solution calculated to safeguard the best interests of manufacturer, distributor and consumer alike.

Reflections on the Rome Conference—I

Salient Trends in Commercial Banking

By Vera Lutz

The International Credit Conference held in Rome last autumn discussed and later published a large body of material of theoretical and practical interest upon banking trends and problems in the forty-eight countries represented.

For the benefit of those who may not see this material, or who cannot spare the time to read it all, THE BANKER *asked Dr. Vera Lutz, the Economic Associate of the Conference, to draw attention to the highlights and comment upon their significance. In this first article she surveys recent trends in commercial banking; a second article will deal with the problem of combating inflation.*—ED.

THE International Credit Conference, which was held in Rome under the auspices of the Italian Bankers' Association between October 18 and 24, 1951, gathered together commercial bankers from forty-eight countries, along with a number of representatives of Central Banks, bank and university economists, and lawyers.

The agenda covered two groups of subjects. The first,* with which alone we shall be concerned in this and a subsequent article, was entitled " Bank Liquidity and the Control of Inflation ". Under this heading the delegates were invited to discuss, in written reports prepared before the Conference opened as well as orally at the Conference sessions, the modern conception of the meaning of bank liquidity, the main features of commercial banking evolution in their respective countries over the past twenty years, and methods of credit control under conditions of inflationary pressure.

Two principal features stand out from the accounts that were given of the important changes that have taken place in the composition of commercial bank assets. The first is the increased importance, in almost all countries, of investments in Government securities and the corresponding decline in lending to private customers compared with the position in 1930; and the reversal of the direction of the movement since 1945 and more especially since the middle of 1950.

In the United States, for example, the movement towards a growing proportion of Government securities, already slightly evident even before 1929, made substantial progress in the depression years as the result of the falling off in private demand for credit on the one hand, and the use of deficit financing as a deliberate anti-inflation device on the other. The movement continued during the war years, when the ordinary effects of war finance were enhanced by the adoption of the system of direct government financing of the expansion of business plant and equipment required by the war effort. Whereas in the middle of 1929 the ratio of loans to total loans and investments (of all commercial banks) stood at over 70 per cent., in the middle of 1945 it was only

* The second subject was " The Financing of Foreign Trade ".

about 20 per cent. A revival of private lending set in after this date and became particularly rapid after the outbreak of the Korean war; by the end of April, 1951, the proportion of loans had in consequence climbed back to 43 per cent.

In other countries the movement has been not dissimilar. Table I indicates for selected countries the way in which the relative importance of Government securities in the assets of the commercial banks has changed over the periods before and after 1945.

"Secondary" Reserve Requirements and Their Effects

In a number of countries the present structure of commercial bank assets is partly conditioned by a new form of legal reserve requirement—obliging banks to hold certain amounts of Government securities—instituted in the post-war years. This new type of regulation was provoked by the banking tendencies just noted: the large amounts of Government securities held by the banks at the end of the war, combined in some cases with the Government's continued heavy demands for funds to finance current budget deficits, on the one hand; and the revival of opportunities for private lending on the other.

Table I

PROPORTION OF GOVERNMENT SECURITIES TO TOTAL ASSETS OF COMMERCIAL BANKS *

(Including compulsory reserves where relevant)

Country	(End-of-year figures, per cent.) 1938	1945	1950
Belgium	18	67	48
France	14	50	15
Italy	30	64	33
Netherlands	15 †	72	56
Sweden	5	24	9
United Kingdom	46	70	63
United States	27	57	36

* Some figures only approximate. † Refers to four large banks only.

At the ruling rates on Government securities, the differential that could be earned by lending to private customers was more than sufficient to compensate for the difference in risk, especially in view of the abnormal assets proportions that prevailed. This situation created a strong inducement in almost all countries for the banks to expand in the direction of lending to private customers rather than to the Government, or even to liquidate part of their existing portfolios of Government securities, either by selling them, or, since they were often partly or mainly short term, simply by not renewing them when they fell due. One way of removing this inducement would have been to offer or allow higher rates of return on Government securities. In some countries (the United States, Sweden and Britain,* for example) this way out was avoided by the process of monetizing the public debt. In others an alternative expedient was employed with the object of maintaining relatively low interest rates on Government borrowing while at the same time avoiding the monetization of the public debt. This method consisted in creating a priority market for Government securities by "blocking" those already held by the banks,

* "Monetization" of debt, in the sense in which the term is used here (implying support for the gilt-edged market to maintain a given yield basis) was abandoned in Britain on the collapse in early 1947 of the Daltonian experiment.—Ed.

and obliging them to invest a certain proportion of future additions to deposits in such securities.

Measures along these lines were introduced in Belgium, Italy, France, and more recently in the Netherlands; and similar measures have been proposed in the United States. The actual formulae in force in the various countries differ considerably in detail. Particular attention may be drawn here to the cases of Belgium and the Netherlands, which exemplify the limitations of such methods, and also the considerable burden that, in their more extreme forms, they may impose upon the commercial banks.

In Belgium ratios of obligatory cover in Government securities against deposit liabilities were introduced early in 1946. In spite of certain recent modifications, the present ratio is very high (50 per cent. or more of sight deposits *plus* time deposits with terms or periods of notice of up to two years), and it is the more severe in its effect on bank earnings in that the regulations specify that the cover must, with limited exceptions, consist of short-term securities (maturities of one year or less), which carry interest rates of less than 2 per cent. Given the present opportunities for private lending at much higher rates, the existing law is regarded as imposing an unfair levy on the commercial banking system. In France and Italy the regulations are much less severe.

In the Netherlands a regulation " blocking " bank holdings of Government securities was imposed in January, 1951. In this instance the regulation simply served, however, to divert the private loan business at the higher interest rates to other lending institutions (such as insurance companies, savings banks and mortgage banks) which were not subject to the regulation. These institutions sold Government securities, with the result that their prices fell; and as the Government was still unwilling to finance refunding operations on the higher yield basis, it turned to the Netherlands Bank for accommodation. Hence, though the new regulation doubtless prevented interest rates on Government securities from rising as high as they would otherwise have done, it failed to prevent the rise entirely and failed also to prevent an increase in the total volume of credit. At the same time it discriminated against the commercial banks by obliging them to hold the less profitable assets while allowing the " institutional " investors to hold the more profitable ones.

It was also predicted during the Conference discussions that, in the United States, given the high proportion of outstanding Government securities held by non-bank investors (some 60 per cent.), recent proposals made there for the introduction of similar restrictions on the free choice of assets by the commercial banks would likewise have failed in their purpose of preventing both a rise in the interest rates on Government securities and an increase in the volume of money.

Development of the " Term " Loan

The second notable change in the character of bank assets arises from the tendency in a number of countries to break away from the traditional concept of commercial banking that excluded medium and long-term loans. This development took place in response to at least two dissimilar causes. In America it was the search for lending opportunities in the 'thirties, when the demand for credit was low, that brought into being the " term " loan. At the end of 1950 about one-third of all commercial and industrial loans out-

standing in the United States represented term loans (i.e. loans with maturities of over one year); and it was calculated in 1946 that about one-half of the term loans had maturities of over five years. Associated with this new form of lending was the introduction of the practice of requiring borrowers to amortize loans by instalments.

In other countries the tendency for banks to undertake longer term lending is mostly a post-war development associated with the condition of the capital market. The difficulty of raising funds by issuing securities to the public, as well as the drying up, through taxation and other causes, of internal and "family" sources of funds, has forced business firms, both large and small, to look increasingly to the banks for finance. A particularly serious case is that of Germany, where the long-term capital market has been almost non-existent since the war.

In France, where discounts of commercial bills at three months or less have continued to be the predominant form of bank credit, medium term credits of up to five years have now become quite common; it was estimated that in March, 1951, they accounted for about 15 per cent. of the total of commercial loans and discounts of the French deposit banks. A change has also recently been made in French law modifying the rules concerning the

TABLE II

RATES OF INTEREST ON DEPOSITS

Country	Demand deposits	Time deposits	Term or period of notice to which maximum rate applies
	(Rates per cent.)		
Belgium	0.50	0.85–2.50	2 years
Denmark	0.25–0.50	3.50–4.00	6 months
France *	0.25–0.50	1.00–2.75	1 year
Germany	1.00–1.50	3.25–5.00	1 year
Italy *	0.50	1.50–2.00	6 months
Netherlands	0.50	1.00–2.50	1 year
Sweden	—	1.00–3.00	6 months
Switzerland	0.00–0.50	1.125–1.75	1 year

* The rates quoted are the "official" rates; considerably higher rates than these are currently being paid by some banks, especially on large deposits.

mortgaging of working stock in order to make it easier for small and medium-size firms that do not qualify for unsecured credits to provide security for obtaining medium-term credits.

The tendency for commercial banks to undertake what is formally recognized as medium-term loan business has also been sanctioned by a corresponding widening of the "eligibility" rules of central banks. Thus in the United States the definition of eligibility was extended in the 'thirties to include term loans. And in France the definition has recently been widened to include medium-term credits.

Even where loans and overdrafts are still formally short-term credits they show a tendency to become in effect longer-term by virtue of repeated renewals, especially because it is less common than formerly for them to be repaid out of the proceeds of capital issues for which they are merely "anticipatory credits".

On the deposits side, a feature that distinguishes continental from English practice is the variety of types of deposit account offered by commercial banks in most continental countries, and the importance in some of them of long-term deposit business. Table II shows the range of interest rates paid for

demand deposits, and for time deposits of various periods, in selected countries at the end of 1950 or beginning of 1951.

As regards the volume and structure of deposit business, it was noticeable in the great majority of countries that the aggregate volume of commercial bank deposits had failed to keep pace with other economic indices (i.e. that their real value was lower than before the war), and that the proportion of medium- and long-term deposits had fallen. In Italy, for example, the real value (calculated on the basis of a 50-fold increase in the price level since 1938) of total deposits at the commercial banks in April, 1951, was still only 81 per cent. of the level of 1938. And while the real value of the deposits that roughly correspond to checking or current accounts (the *conti correnti di corrispondenza*) had risen to 125 per cent. of their 1938 level, thus increasing more or less in proportion to the level of production, the real value of those that are essentially in the nature of savings (the *depositi fiduciari*) was only 62 per cent. of the 1938 level. Similar movements were shown by the statistics given for Belgium. These movements were attributed to several factors. A tendency still persisted in some countries for the public to hold a higher proportion of currency to bank deposits than before the war. Thus in Belgium the ratio of bank deposits to notes was only 64 per cent. at the end of March, 1951, as compared with an average of 87 per cent. for the years 1936-38. More important than this was the fact that the public can only slowly restore its savings (in the form of time and savings deposits) to the old real level after they have been destroyed by inflation. In some instances, too, there was a third factor at work: the increasing competition with the commercial banks from other institutions that take deposits, such as the postal savings systems and other semi-public institutions, as well as the private savings banks.

More normal relationships in the deposits structure of the commercial banks are, however, slowly re-establishing themselves. And in some instances there are signs that time and savings deposits may, for some time at least, become the preferred medium of saving, along with insurance, for private savers, and that public subscriptions to security issues will continue to play a much smaller rôle than formerly. To some extent this phenomenon is associated with restrictions on the capital market that can be removed (e.g. interest rate " stops " and dividend limitations), and to some extent it is due to the effect of taxation in reducing the importance of the large saver; but it is also due to a preference on the part of an inflation-conscious public for keeping its savings in an easily mobilizable form allowing them to be quickly withdrawn for conversion into goods. (It should be noted in this connection that in most countries time deposits as well as savings deposits may be drawn on, up to a certain amount or on payment of a commission, before the expiry of the term or period of notice.)

If this situation continues it will mean that the banks will hold on deposit the funds that people would under other circumstances have invested directly in the long-term securities market, and that they may thus be obliged to take over the financing of industry to a greater extent than formerly: this is merely the other side of the medal that we presented earlier in speaking of the changes that have actually taken place in bank lending practices. A possible consequence is that in some countries the commercial banks may find themselves occupying an intermediate position between that of banks with strictly short-term business (both on the assets and on the deposits side), and

that of the " mixed banks " which existed over a large part of the Continent until they were superseded in the early 'thirties by a strict division between the ordinary deposit or commercial banks on the one side, and *banques d'affaires* and other institutions specializing in medium- and long-term credit on the other.

Changing Views about Bank Liquidity

The discussion of the theory of bank liquidity covered ground that will be fairly familiar to most English readers. It pointed to the change in emphasis from the original idea that liquidity (defined as " the possibility of turning an asset into cash quickly and without loss ") was an intrinsic quality of a particular type of asset, best represented by the so-called " self-liquidating " type of which the " classical " form was the commercial bill, towards the idea that liquidity was synonymous with " shiftability ". Two cases of shiftability needed to be distinguished. The first was where a single bank suffered a drain of cash (withdrawal of deposits) to other banks, and in that case assets were liquid if they could ultimately be shifted to those other banks. The second case was where the commercial banking system as a whole suffered a drain of cash (to the public), and in that case liquidity meant the possibility of shifting assets to the Central Bank, against the creation by the latter of additional cash. It was to this second case that most importance was now generally attached.

The notion that the Central Bank alone can guarantee the liquidity (in the sense defined) of the banking system as a whole—a notion that in its essentials goes back to Bagehot—implies that no asset, except cash itself, is inherently more liquid than any other; the difference depends only on the Central Bank's willingness or unwillingness to " monetize " the asset concerned. What remains as a difference between " short "- and " long "-term assets—a difference in " liquidity " in a much wider sense—is then: (*a*) the opportunity that short-term lending gives the bank of revising its lending terms (i.e. raising interest rates) should market conditions change; and (*b*) the greater ease with which a banker can judge the credit-worthiness of a customer, and therefore the " solvability " of a loan to that customer, over a short period than over a long.

While this view of liquidity was in general accepted, the question was raised whether there was not some danger of its being over-emphasized. It was pointed out, first, that in a system of unit banks, some of which by virtue of their location specialize in particular types of deposit business, individual banks may suffer substantial reductions in deposits for sustained periods even though no reduction is taking place in the system as a whole. Thus an American delegate observed that it was still important that a bank with specially volatile deposits should hold an amount of short-term assets sufficient to cover possible withdrawals without recourse to borrowing from the Central Bank. It was also noticeable that considerably more importance was attached to this aspect of the liquidity problem in some continental countries than, for example, in Britain.

The second danger emphasized was that this concept of liquidity might create an attitude of too great a reliance on the Central Bank. This question will be discussed in the second of these two articles, which will survey the reactions of the Conference to the problem of combating inflation.

Publications

The Banking Mechanism

One of the very few statements in this book* about which it is possible to entertain serious doubts appears on the dust-jacket, where it is indicated that it is designed not only for the student, but for the "intelligent layman". It is pleasant to think of Mr. Dacey (or his publishers) retaining so favourable a view of the intelligence of the human race; for the book needs close and careful reading even by those already reasonably well acquainted with the subject matter, and will prove quite a tough enough morsel to digest for most second-year, and indeed for many third-year, university students of economics.

The difficulty of the book is in no way the author's fault; but the inherent complexity of the subject and the degree of condensation, presumably due to limitations of space, sometimes combine to tax even Mr. Dacey's lucidity of style. There are not many books of which it can be said that they would be better if they were longer, but it can be said of this one.

The general contents of the book are adequately indicated by its title. It is not primarily a study of institutions; nor is its interest mainly historical. It is a very thorough and careful examination, based both on a knowledge of the facts and a wide grasp of some of the more difficult parts of economic theory, of the ways in which the system has worked in the past and works to-day (or at any rate yesterday). It contains only enough institutional information to make the argument intelligible, while the very valuable historical chapters with which the book concludes are strictly selective in their material and are devoted to developing the analysis rather than to providing information for its own sake. While the beginner will probably find it necessary to read more elementary books before tackling this one, when he is able to do so he will find many of his uncertainties cleared up. In particular, the treatment of the relationship between open market policy and bank rate policy, and of the significance of changes in the volume of bank deposits in a controlled economy, is most illuminating.

Apart from over-compression, there are very few faults to be found even on minor points. On page 81 Mr. Dacey says that Diagram 6 shows advances as 45 per cent. of deposits; in fact (since the notation reads from the top down), it shows them as 55 per cent. On page 99 he says that "periods of bill famine will be apparent at a glance from the chart" (Diagram 8). No doubt the chart Mr. Dacey had before him when he was writing was on a larger scale; with the one in the book it took a good many glances even to be sure which line was which, and a few more sentences to help the reader in the interpretation of it would greatly have increased its value. In a number of places, such as the last paragraph of page 110, it is difficult to be sure what is meant by "before the war"; here I think it means "before 1914", but I may be wrong. And on page 147 it is implied that Bank rate was raised to 6 per cent. before, instead of after, the 1931 departure from the gold standard. But these are very small blemishes on a book which I can emphatically recommend to all those who wish to make a serious study of the subject and are prepared to overcome the difficulties of really understanding it. To many university students, both internal and external, it will come as a godsend.

In conclusion, may I express the hope that in the not too distant future there may be a second edition in which Mr. Dacey may be allowed to spread himself a little, even if it means his overflowing into two volumes. He will in any case need extra room to deal with all that has happened, and will have happened, since the end of 1950.

F. W. PAISH.

* *The British Banking Mechanism.* By W. Manning Dacey. (Hutchinson's University Library, 1951, pp. 203. 8s. 6d.)

International Banking Review*

Belgium

UNDER a new agreement with the Council of the O.E.E.C. Belgium is to receive from the European Payments Union a maximum of $60 millions in gold in settlement of possible payments surpluses with the E.P.U. countries during the first three months of 1952. For any surplus in excess of this amount she will be required to extend credit facilities. The Council has recommended Belgium to apply export restrictions in a way that will cause the least prejudice to her O.E.E.C. partners and not to abolish unilaterally her export commitments for certain products.

Exporters have been warned that in trading transactions with the other E.P.U. countries the granting of a licence does not mean that they will be certain to collect payment in Belgian francs.

Brazil

A new Government decree stipulates that remittances of business earnings in excess of 8 per cent. of registered foreign capital will be regarded as remittance of capital and will be deducted from the amount of registered foreign capital. The new decree applies retrospectively to remittances in excess of 8 per cent. already made.

Parliamentary approval has been secured for a bill authorizing the Federal Government to guarantee, up to a limit of U.S. $500 millions, money borrowed from abroad to finance the capital development programme. The measure also provides for a Federal Government guarantee up to U.S. $250 millions for foreign loans secured by Brazilian States, municipalities and public utility concerns for the execution of public works.

British West Africa

The report of the British West African Currency Board for the year to June 30, 1951, shows that the amount of the Board's currency in circulation rose during the year by £12.5 millions to £78.9 millions. In the previous year the issue declined by £1.7 millions. Of the notes outstanding at the end of June, 1951, £13.2 millions were in the hands of the banks and £65.7 millions with the general public. The respective figures a year earlier were £14.5 millions and £51.5 millions.

The latest increase in the note circulation in West Africa is attributed largely to the rise in the prices of the region's main products in the period after the opening of the war in Korea.

Burma

The Premier, Mr. Thakin Nu, has announced Burma's acceptance of the British suggestion that it should participate in the Colombo Plan for the economic development of South and South-East Asia.

Burma has become a member of the International Monetary Fund and the International Bank for Reconstruction and Development. The country's quota in the Fund has been fixed at $15 millions, while it is subscribing to 150 shares of capital stock in the World Bank with a value of $15 millions.

Canada

The Minister of Trade and Commerce, Mr. Howe, has announced that capital investment rose from $3,800 millions in 1950 to $4,600 millions in 1951, a new

* Other current international banking news is discussed in "A Banker's Diary", on pages 65-70.

all-time high figure. He also stated that inflationary pressures had slackened in the second half of the year as the Government's anti-inflationary programme gathered momentum.

The Minister claimed that the deficit in the Dominion's external trade was attributable to increased purchases of arms from the United States and a high demand for U.S. consumer and capital goods. It was not a reflection of any basic weaknesses in the country's economy.

Hire-purchase credit restrictions imposed in 1951 have been modified by extending the period during which such transactions may be completed from 12 to 18 months. Certain goods have also been placed outside the scope of the restrictions imposed in October, 1951.

Chile

As a result of a further overhaul of the exchange structure, imports at the official rate of 31 pesos per U.S. dollar are in future to be restricted to newsprint and sugar. The preferential rate of 43 pesos, which previously applied to certain classes of imports, has been abolished.

The banks are now required to apply to the National Council of Trade before purchasing free market exchange for non-trade operations that involve amounts equivalent to more than £100.

France

The note circulation of the Bank of France reached the all-time high level of Frs. 1,842,000 millions at the end of 1951. This represented an increase of 18 per cent. when compared with the total for a year before. The growth of inflationary pressures is also strongly reflected in the expansion of discounts and other credits granted by the Bank of France. Thus at the end of 1951 discounts were standing at Frs. 773,000 millions, against Frs. 427,000 millions a year earlier, and the bank's total credits at Frs. 1,037,000 millions against Frs. 581,000 millions.

Germany

A syndicate of banks and commercial institutions has established a new banking institution—the Export Financing Corporation—to provide finance for German medium and long-term exports. Hitherto such exports have been financed largely on credit furnished by the Federal Bank, but this institution has recently shown some reluctance to renew existing lines of credit. The new bank, which has been approved by the German Credit Control Board, will have an initial working capital of Dm. 200 millions. In addition to a share capital of Dm. 20 millions, the bank

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will have at its disposal 2 to 3 per cent. of the deposits of the founder banks. It is intended to double the working capital later by raising the share capital to Dm. 40 millions, which should attract another Dm. 180 millions of the founder banks' deposits to the bank. The new institution will have its headquarters in Frankfurt. The cost of its credit will be 8 per cent. per annum, this being made up of a rate of interest of $7\frac{1}{2}$ per cent. and a commission charge of $\frac{1}{8}$ per cent. per quarter. Advances may be made up to 80 per cent. of the amount of the security, that is, up to the limit of the State-sponsored credit risk insurance. The bank's promissory notes will be acceptable as collateral by the German Federal Bank but re-discount facilities will be available with the Federal Bank only in emergency.

An analysis prepared by the Bankverein Westdeutschland shows that the Stock Exchange value of all quoted German shares rose by an average of 80 per cent. in 1951. The coal, iron and steel group led the advance with rises of 150 per cent.; banks showed an average advance of 126 per cent.

As a further step towards establishing normal relations with the Western Powers, the West German Government has decided to apply for membership of the Bretton Woods institutions.

The monthly report of the German Federal Bank puts the percentage of imports that will be affected by the new liberalization measures at 57. It expresses the view that the results of these steps will be to return Germany to the position of a debtor of E.P.U., but argues that the currency situation will be kept under full control by means of the new licensing procedure.

India

Under a new Government regulation the authorities have the power to compel residents of India holding controlling shares in foreign companies to bring back to India the earnings of their investments. It also empowers them to require the repatriation of the capital if the companies should go into liquidation. The new law provides that control of a foreign company shall not be transferred to another person without the consent of the Reserve Bank. The central bank's permission is also required before any money is lent to a company controlled by persons resident outside India.

The newly-created Indian Finance Commission has decided that the present system of allocations to the Indian States from the divisible pool of income tax and jute duties shall be maintained for another year. The Commission has been entrusted with the task of appraising the financial needs of every State to enable it to discharge its functions at standards not appreciably below those of other States, to satisfy itself that the States have made reasonable efforts from their own resources to realize this objective, and to find the finance required to meet any deficiencies.

An agreement concluded with the United States provides for the creation of an Indo-American technical co-operation fund with $50 millions to be granted in American currency by the U.S. Government. The money is to be used, with rupee funds set aside by the Indian Government, to finance agreed development projects in India.

Israel

Israel has been granted a $10 million loan by the Bank of America. The advance is secured against the proceeds of the issue of Israeli bonds now being made in the United States.

Japan

An attempt is being made to mop up some of the surplus money now circulating in the economy by the issue of savings bonds. The Government's new bond is a

3-year maturity and it is being issued at a price that will give an effective yield of 6 to 7 per cent.

Netherlands

Under an agreement concluded with a group of American banks headed by the Chase National, the Netherlands is to receive a $15 million loan in U.S. dollars. Arrangements have also been made for a loan of $3 millions by the Bank for International Settlements. Both advances are for a period of two years and carry interest at 3½ per cent.

Economic aid from the United States in the year to June 30, 1952, is now expected to amount to $100 millions.

New Zealand

The Governor of the Reserve Bank, Mr. E. C. Fussell, has announced that a close examination is being made of bank credit facilities in New Zealand to decide whether any specific restrictive action is necessary. Mr. Fussell declared that aggregate trading bank advances were still showing a rising trend and that this, assisted by the high level of demand, was accentuating the tendency for prices to rise. This trend had to be corrected because imports were already outstripping New Zealand's overseas income by a wider margin than could be sustained for long. Many business concerns had been relying too much on the banks to provide working capital and had become under-capitalized, which was undesirable both for the banks and themselves.

The trading banks had been asked to examine all accounts where trading limits exceeded £10,000. In cases where customers were leaning too heavily on the banks, the latter were to provide the Reserve Bank with the necessary particulars to enable it to decide whether action was called for. Also, except with the approval of the Reserve Bank, no increases would in future be granted in importers' credits for the purpose of acquiring overseas funds. Loans to hire-purchase concerns would be examined with a view to securing reductions wherever possible.

Nicaragua

The National Bank of Nicaragua has reported that the adoption of the new methods of exchange control recommended by the International Monetary Fund has been followed by an impressive improvement in the country's balance of payments. Thus in the first half of 1951 short-term obligations for an amount of U.S. $50 millions were discharged and U.S. $10.9 millions added to reserve. The delay in issuing import permits and in making payment for imports has been eliminated. The bank has also asserted that the previous unfairness in the distribution of exchange to importers has been remedied and substantial progress made towards the establishment of a stable currency within the limits set by a free exchange market.

Persia

The President of the Persian Foreign Exchange Commission, M. Behnia, has urged the Government to create a foreign exchange fund with the object of increasing the Commission's control over foreign exchange activities and promoting economic stability. M. Behnia asserted that the reduction in the amount of foreign exchange released by official sources and the withdrawal of convertibility facilities as a result of the oil argument with Britain had been followed by a steep increase in black market activity. His statement also argued that existing sterling and dollar reserves were likely to be used up in a matter of months. If the oil crisis continued it would be necessary to make rigorous economies in foreign exchange

expenditure. New conditions would have to be made for the opening of credits abroad.

The Government has floated a loan for 2,000 million rials (about £22 millions) to help it surmount the financial problems created by the oil crisis.

Portugal

The Budget statement for 1952 provides for total expenditure of 5,966 million escudos, compared with 5,315 millions in 1951. Of the total, 4,636 million escudos is to cover ordinary expenditures and the remaining 1,330 million escudos to finance certain extraordinary expenditures, including 500 million escudos for defence projects that are being undertaken to meet commitments to the North Atlantic Treaty Organization.

South Africa

Agreement has been reached with a group of Swiss banks for a loan to the Union of Swiss Frs. 60 millions. The credit carries interest at 4 per cent. and is redeemable in 12 to 18 years. It is intended that the subscribing banks should subsequently offer the loan for public subscription in Switzerland. All the transfers of moneys arising from the loan operation will be effected outside the machinery of the European Payments Union.

Sweden

The committee appointed by the Minister of Finance to find ways of mopping up excess purchasing power and defeating inflation has proposed an excess profits tax to be levied retrospectively, starting with 1951 earnings. The tax would be applied to the difference between the earnings of business and forest owners in 1949 and 1951. In the case of business concerns, 30 per cent. of the difference would be regarded as not liable to tax on the assumption that it had been spent on "rationalization". The remaining 70 per cent. would bear a tax of 40 per cent. The rates of tax applicable to forest owners are slightly different.

A new trade agreement has been signed with the United Kingdom covering exchanges between the two countries in 1952.

Switzerland

The official ruling that gold sales effected through banks and other professional dealers shall continue to be subject to the 4 per cent. turnover tax is expected to make it impossible for banking institutions to take advantage of the relaxation of official restrictions on dealings in gold. It has been pointed out that it is impossible for the banks to bear the tax themselves because the 4 per cent. tax is greater than the spread between the buying and selling prices for gold.

Turkey

The Government has announced that it will not make use in 1952 of the credit of £T 1 million that the Ottoman Bank is required to extend annually by virtue of its concession. It has also stated that the position of the bank is being examined in connection with the law for the encouragement of foreign capital. An amendment of the bank's concession is expected to be made when it comes up for renewal this year.

Uruguay

The Government has restricted imports from certain currency areas by suspending the acceptance of "sworn declarations", covering imports to be made from these areas under contracts concluded but not liquidated up to December 3,

1951. The restrictions were at first applied to imports from sterling sources, but were later modified to permit the import of most " first-category " goods from the United Kingdom. The official decision is the result of a shortage of dollars and certain other currencies caused by heavy imports in recent months. Uruguayan reserves of sterling, however, are fairly substantial.

Yugoslavia

With effect from the last day of 1951 the Yugoslav dinar has been devalued to a new gold parity of 2.96223 milligrams of gold. This gives the dinar a value of 300 to the U.S. dollar, compared with 50 previously. In terms of sterling its value changes from 140 to 840. The adjustment is part of the general overhaul of the Yugoslav economic structure that is being carried out with the advice and assistance of the American and British Governments. It is intended to give the dinar a " realistic " foreign exchange value.

Appointments and Retirements

MIDLAND'S NEW CHAIRMAN

The directors of the Midland Bank have announced the election of their former deputy chairman, Lord Harlech, as chairman of the bank in succession to the late Lord Linlithgow. As Mr. G. W. A. Ormsby-Gore, Lord Harlech had a distinguished political career between the wars, being Postmaster-General in 1931 and Secretary of State for the Colonies from 1936 to 1938. During the war he was Regional Commissioner for the North-East and, later, British High Commissioner in South Africa. He has been a director of the Midland since 1944; both his father and his grandfather were on the board of the old London Joint Stock Bank, which amalgamated with the Midland group in 1918.

LORD LINLITHGOW

The City, and many outside the City, will share with the directors of the Midland Bank their " deep sorrow and sense of loss " at the sudden death of Lord Linlithgow, who collapsed and died while out with a shooting party on his estate in Scotland on January 5. Lord Linlithgow was, of course, chiefly known to the world at large as the able and respected Viceroy of India during the delicate years of crisis from 1936 to 1943. He became chairman of the Midland in February, 1945, and was president of the British Bankers' Association in 1948 and 1949. His mastery of the art of committees made him a valued recruit to the banking world, which he joined so late in life.

Barclays Bank—*Birmingham District, Local Head Office:* Mr. W. N. Ritchie, from Luton, to be a local director. *Windsor District, Local Head Office:* Mr. C. E. Brooke, from Birmingham, to be a local director. *Pall Mall and Fleet St. (Goslings) District, Local Head Office:* Mr. H. H. Hutchinson to be district manager. *Advance Dept.:* Mr. R. Lewis, from 366 Strand, to be a controller of advances (London district). *Inspection Dept.:* Mr. A. Rawlings, from Pall Mall and Fleet St. (Goslings), to be joint chief inspector. *Trustee Dept., City:* Mr. E. J. Ellmore, from City branch, to be manager. *Trustee Dept., East London:* Mr. D. W. S. Woodley to be manager. *Trustee Dept., North-West London:* Mr. A. R. Turner, from East London branch, to be manager. *Trustee Dept., Oxford:* Mr. E. G. Gibson, from North-West London branch, to be manager. *Chief Foreign:* Mr. M. R. Gravatt to be deputy manager. *Bromley:* Mr. A. Bourneman, a controller of advances (London district), to be manager. *Dulwich East,* 393 *Lordship Lane:* Mr. J. H. Morris to be manager. *Ascot:* Mr. S. J. Maskell, from Hayes, to be manager. *Bridlington Quay:* Mr. W. Batty, from Filey to be manager. *Filey:* Mr. E. D. Pritchett, from Tadcaster, to be manager. *Tadcaster:* Mr. G. E. Sylvester, from Riby Sq., Grimsby, to be manager. *Uppingham:* Mr. G. C. Thomas, from Gallowtree Gate, Leicester, to be manager. *Windsor:* Mr. G. L. Shephard, from Ascot, to be manager.

Clydesdale & North of Scotland Bank—*Ballater:* Mr. J. Hay, from Aberdeen, to be manager in succession to the late Mr. H. M. Williams.
District Bank—*Ashton-under-Lyne:* Mr. R. W. Wilson, from Cardiff, to be manager. *Manchester and Salford, Higher Openshaw:* Mr. H. Boyle to be manager.
Gillett Bros. Discount Co.—Mr. Hugh Mansfield O'Connor has been appointed deputy chairman.
Lloyds Bank—*Branches Stock Office:* Mr. L. C. Peace to be manager on retirement of Mr. H. S. L. Snell. *Chief Inspector's Dept.:* Mr. V. Bruce-Jones, from Barnet, to be an inspector.
Martins Bank—*London Foreign Branch:* Mr. R. Davidson has been appointed Foreign manager in succession to Mr. A. H. Birse, C.B.E. Mr. H. C. Horton to be sub-manager. Mr. E. P. Jaggard to be assistant manager. *Bath:* Mr. G. E. Clarkson to be manager. *Birmingham:* Mr. J. C. Wood to be manager. *Huddersfield, Westgate:* Mr. T. Haighton to be manager. *London—Gracechurch St.:* Mr. R. A. Machell to be manager; *Holborn:* Mr. E. A. E. Livsey to be manager. *Manchester, Deansgate:* Mr. E. J. Cutler to be manager.
Midland Bank—*Head Office:* Mr. J. E. Johnson, from Sheffield, to be a superintendent of branches. *Bilston:* Mr. S. Thewlis, from Snow Hill, Birmingham, to be manager in succession to Mr. H. F. Williams. *Birmingham, Snow Hill:* Mr. H. W. Drury to be manager. *Evesham:* Mr. H. F. Williams, from Bilston, to be manager on the retirement of Mr. C. F. Carter. *Grantham:* Mr. H. Hughes, from Coventry, to be manager on the retirement of Mr. S. T. Starbuck. *Prestatyn:* Mr. G. W. Rees, from Monmouth, to be manager on the retirement of Mr. D. D. Davies.
National Provincial Bank—The Rt. Hon. Ralph Assheton, M.P., and Mr. Seymour John Louis Egerton have been appointed directors. *Head Office:* Mr. A. C. Irwin, principal, Staff Training Centre, to be staff controller. Mr. P. G. S. Mann, a controller, advance dept., to be a joint chief controller. *Smiths Office, Lombard St.:* Mr. W. C. Cooper, from Baker St., to be manager in succession to Mr. J. R. Coombe. *Baker St.:* Mr. A. L. Virgo, from Southwark, to be manager. *Bow:* Mr. H. T. Lathrope to be manager in succession to the late Mr. A. S. Neale. *Chorley Wood:* Mr. C. G. Hearsey to be manager in succession to Mr. E. A. Walton, who has retired. *Colwyn Bay:* Mr. D. E. Price, from Prestatyn, to be manager in succession to Mr. T. M. Thomas. *Dartmouth:* Mr. H. G. Thompson, from Exeter, to be manager. *Old Swan, Liverpool* (constituted a full branch of the Bank): Mr. H. C. Sergent to be manager. *Monmouth:* Mr. R. P. B. Thomas, from Monmouth, to be manager in succession to Mr. R. J. Barrow. *West Bridgford, Nottingham:* Mr. N. J. Chittenden to be manager. *Portmadoc:* Mr. R. W. D. Parry to be manager in succession to Mr. J. E. Roberts. *Portsea:* Mr. P. G. Jolliffe, from Dartmouth, to be manager in succession to Mr. F. A. Norman. *Prestatyn:* Mr. D. G. Davies, from Bangor, to be manager. *Rhos-on-Sea:* Mr. T. J. Thomas, manager, has retired. *Scunthorpe:* Mr. C. P. Hulme, from West Bridgford, Nottingham, to be manager in succession to Mr. D. Davies. Mr. E. H. Jones, from Derby, Mr. G. G. Price, from Wrexham, and Mr. J. E. Holifield, from Bradford, to be inspectors of branches.
Westminster Bank—*Head Office:* Mr. W. T. Lawrence, manager at Mark Lane (Corn Exchange), to be an inspector of branches. Mr. D. M. Liddington, from Croydon, to be a controllers' assistant. *Trustee Dept., Threadneedle St.:* Mr. G. E. M. Jenkins, manager, Piccadilly Trustee branch, to be an assistant manager. *Llandudno:* Mr. G. J. Bowman to be manager. *Mark Lane (Corn Exchange):* Mr. W. E. Edwards, from Lothbury office, to be manager. *Piccadilly Trustee Branch:* Mr. H. D. G. Trew, from Trustee Dept., Threadneedle St., to be manager. *Rhyl and Prestatyn:* Mr. G. E. Williams, from Llandudno, to be manager on retirement of Mr. L. L. Jones.

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BANK ADVANCES IN GREAT BRITAIN*

(LATEST QUARTERLY STATEMENTS)

Group	February† 1946		November 1950		February 1951		May 1951		August 1951		November 1951	
	£000's	% of total	£000's	% of total	£000's	% of total	£000's	% of total	£000's	% of total	£000's	% of total
1. Coal Mining	8,925	1.1	5,347	.3	5,163	.3	5,055	.3	3,681	.2	2,963	.1
2. Quarrying, etc.	2,328	.3	4,118	.2	4,858	.3	4,936	.3	5,222	.3	4,659	.2
3. Iron and Steel & Allied Trades	15,353	1.8	19,153	1.1	21,139	1.2	16,295	.9	14,275	.7	17,645	.9
4. Non-ferrous Metals	1,978	.2	5,147	.3	7,556	.4	7,125	.4	4,068	.2	5,430	.3
5. Engineering, etc.	66,557	7.8	92,391	5.5	98,791	5.5	100,570	5.3	111,826	5.7	126,734	6.3
6. Shipping and Shipbuilding	10,318	1.2	15,460	.9	17,313	1.0	16,713	.9	15,826	.8	13,485	.7
7. Transport and Communications	9,570	1.1	16,076	1.0	17,423	1.0	16,965	.9	15,818	.8	17,304	.9
8. Cotton	7,091	.8	8,639	.5	10,104	.6	9,386	.5	14,075	.7	13,780	.7
9. Wool	4,315	.5	21,005	1.2	38,619	2.1	39,803	2.1	40,755	2.1	28,768	1.4
10. Other Textiles	10,232	1.2	33,034	2.0	45,207	2.5	43,327	2.3	52,506	2.7	61,274	3.0
11. Leather and Rubber	4,925	.6	13,947	.8	17,604	1.0	23,123	1.2	23,153	1.2	22,029	1.1
12. Chemicals	9,185	1.1	16,715	1.0	19,212	1.1	21,513	1.1	25,327	1.3	39,286	1.9
13. Agriculture and Fishing	66,489	7.8	171,220	10.2	177,877	9.8	184,304	9.7	202,015	10.3	197,443	9.8
14. Food, Drink, and Tobacco	57,230	6.8	130,540	7.8	127,669	7.1	143,694	7.6	135,099	6.9	164,435	8.2
15. Retail Trade	62,248	7.3	179,353	10.7	191,836	10.6	210,087	11.1	212,833	10.8	213,808	10.6
16. Entertainment	26,731	3.2	28,854	1.7	29,582	1.6	29,340	1.5	27,764	1.4	26,856	1.3
17. Builders and Contractors	38,770	4.6	62,933	3.7	66,587	3.7	72,094	3.8	73,503	3.7	70,136	3.5
18. Building Materials	4,988	.6	14,587	.9	15,254	.8	16,498	.9	19,755	1.0	20,687	1.0
19. Unclassifiable Industry and Trade	27,926	3.3	95,627	5.7	106,478	5.9	112,802	6.0	130,185	6.6	135,422	6.7
20. Local Government Authorities	78,696	9.3	93,825	5.6	90,437	5.0	89,765	4.7	99,208	5.0	87,544	4.3
21. Public Utilities (other than Transport)	7,285	.9	42,009	2.5	55,888	3.1	78,138	4.1	70,758	3.6	94,338	4.7
22. Churches, Charities, Hospitals, etc.	10,369	1.2	11,559	.7	11,703	.6	12,637	.7	13,222	.7	13,339	.7
23. Stockbrokers	4,081	.5	5,195	.3	5,646	.3	6,613	.3	6,233	.3	7,157	.4
24. Other financial	73,168	8.6	178,907	10.6	194,195	10.7	201,103	10.6	209,668	10.7	195,736	9.7
25. Personal and Professional	239,549	28.2	417,594	24.8	430,675	23.8	432,977	22.8	437,648	22.3	435,927	21.6
TOTALS	848,307	100.0	1,683,235	100.0	1,806,816	100.0	1,894,863	100.0	1,964,423	100.0	2,016,185	100.0

* Including all members of British Bankers' Association. † Date of first classification in new post-war series.

Banking Statistics

National Savings

(£ millions)

	Savings Certificates (net)	Defence Bonds (net)	Savings Banks (net)*	Total Small
1947 II ..	40.3	– 3.7	– 19.6	17.0
III ..	2.7	– 19.8	2.9	– 14.2
IV ..	16.4	– 25.1	17.2	8.5
1948 I ..	29.4	– 29.9	54.6	54.1
II ..	– 2.3	– 31.2	13.7	– 19.8
III ..	– 4.5	– 20.3	6.4	– 18.4
IV ..	– 7.2	– 5.8	8.3	– 4.7
1949 I ..	7.3	– 1.4	52.2	58.1
II ..	– 1.5	– 0.4	8.6	6.7
III ..	– 7.6	– 4.8	– 2.7	– 15.1
IV ..	– 8.9	– 5.1	– 3.2	– 17.2
1950 I ..	– 5.5	– 9.1	36.6	22.0
II ..	–10.9	– 9.6	6.4	– 14.1
III ..	–13.6	– 7.5	– 2.4	– 23.5
IV ..	– 8.6	– 7.3	– 4.3	– 20.2
1951 I ..	27.5	3.9	3.3	34.7
II ..	15.3	– 0.1	– 28.9	– 13.7
III ..	1.0	– 10.3	– 11.5	– 20.8
IV ..	0.5	– 19.9	– 1.0	– 20.4

	Savings Certificates (net)	Defence Bonds (net)	Savings Banks (net)*	Total Small
1949 Dec. ..	– 4.2	– 1.9	–12.7	– 18.8
1950 Jan. ..	– 0.6	– 1.8	17.6	15.2
Feb. ..	– 3.2	– 2.6	13.0	7.2
Mar. ..	– 1.7	– 4.7	6.0	– 0.4
April ..	– 2.5	– 3.2	8.7	3.0
May ..	– 3.8	– 3.4	0.4	– 6.8
June ..	– 4.6	– 3.0	– 2.7	– 10.3
July ..	– 4.7	– 2.5	– 6.7	– 13.9
Aug. ..	– 4.1	– 2.3	– 0.8	– 7.2
Sept. ..	– 4.8	– 2.7	5.1	– 2.4
Oct. ..	– 1.2	– 2.2	8.8	5.4
Nov. ..	– 3.0	– 2.7	3.7	– 2.0
Dec. ..	– 4.4	– 2.4	–16.8	– 23.6
1951 Jan. ..	– 1.5	– 2.0	15.0	11.5
Feb. ..	19.3	2.1	– 5.9	15.5
Mar. ..	9.7	3.8	– 5.8	7.7
April ..	7.7	– 0.2	– 1.4	6.1
May ..	2.7	– 0.1	–14.7	– 12.1
June ..	4.9	0.2	–12.8	– 7.7
July ..	1.2	– 0.7	–16.8	– 16.3
Aug. ..	– 0.5	– 5.1	– 4.6	– 10.2
Sept. ..	0.3	– 4.5	9.9	5.7
Oct. ..	1.0	– 7.3	12.3	6.0
Nov. ..	– 0.3	– 5.7	3.8	– 2.2
Dec. ..	– 0.2	– 6.9	–17.1	– 24.2

* Including Release Benefit Accounts from July, 1945.

Ordinary Revenue and Expenditure

Year to Mar. 31:	Ord. Exp. £m.	Ord. Rev. £m.	Deficit £m.
1938 ..	898.1*	872.6	25.5*
1939 ..	1054.8*	927.3	127.5*
1940 ..	1809.7*	1049.2	760.5*
1941 ..	3867.2	1408.9	2458.3
1942 ..	4775.7	2074.1	2701.6
1943 ..	5623.2	2819.9	2803.3
1944 ..	5788.4	3038.5	2749.9
1945 ..	6057.8	3238.1	2819.7
1946 ..	5474.8	3284.5	2190.3
1947 ..	3910.3	3341.2	569.1
1948 ..	3187.1	3844.9	657.8†
1949 ..	3152.8	4006.6	853.8†
1950 ..	3356.6	3924.0	567.4†
1951 ..	3238.0	3977.8	739.9†

By Quarters:	Ord. Exp. £m.	Ord. Rev. £m.	Deficit £m.
1948 III ..	751.4	831.7	80.2†
IV ..	791.4	802.7	11.3†
1949 I ..	996.2	1577.9	581.7†
II ..	754.0	756.7	2.8†
III ..	833.0	820.7	12.3
IV ..	823.7	811.0	12.7
1950 I ..	946.0	1536.3	590.3†
II ..	725.2	768.8	43.5†
III ..	778.2	813.3	35.1†
IV ..	803.7	791.6	12.1
1951 I ..	930.8	1604.2	673.4†
II ..	829.6	846.0	16.4†
III ..	971.2	938.6	32.6
IV ..	1090.6	898.7	191.9

*Allowing for loan expenditure. † Surplus.

Floating Debt

	Jan. 20, 1951 £m.	Dec. 31, 1951 £m.	Jan. 5, 1952 £m.	Jan. 12, 1952 £m.	Jan. 19, 1952 £m.
Ways and Means Advances:					
Bank of England	—	5.8	—	—	—
Public Departments	395.8	252.5	267.7	256.8	277.8
Treasury Bills:					
Tender	3220.0	4782.9	4700.0	4723.4	4943.5
Tap	1844.6				
Treasury deposit receipts	445.0	119.0	116.5	80.5	80.5
	5906.4	5160.1	5144.2	5060.7	5001.8

* Including all members of British Bankers' Association. † Date of first classification in new post-war series.

Treasury Deposit Receipts

		Raised £m.	Redeemed £m.	Outstanding† £m.
1949	Dec. 31*	260.0	142.5	872.0
1950	March 31	—	29.5	465.0
	June 30	140.0	190.0	350.0
	Sept. 30	55.0	—	505.0
	Dec. 31	100.0	139.0	525.0
1951	March 31	90.0	146.5	283.5
	May 26	75.0	75.0	319.5
	June 30	50.0	25.0	344.5
	July 28	—	—	344.5
	Aug. 25	35.0	54.5	325.0
	Sept. 30	90.0	125.0	290.0
	Oct. 27	—	115.0	175.0
	Nov. 24	—	50.0	125.0
	Dec. 31	—	6.0	119.0

* Periods ended on last Saturday in each month, except at final month in each quarter.
† The T.D.R. issue reached its highest level on September 7, 1945, at £2225 millions.

1951 Week ended:	Raised	Redeemed	Net New Borrowing
July 14 ..	—	—	—
,, 21 ..	—	—	—
,, 28 ..	—	—	—
Aug. 4 ..	—	—	—
,, 11 ..	35.0	—	35.0
,, 18 ..	—	24.5	– 24.5
,, 25 ..	—	30.0	– 30.0
Sept. 1 ..	—	35.0	– 35.0
,, 8 ..	40.0	40.0	—
,, 15 ..	—	25.0	– 25.0
,, 22 ..	25.0	25.0	—
,, 30 ..	25.0	—	25.0
Oct. 6 ..	—	40.5	– 40.5
,, 13 ..	—	25.0	– 25.0

1951 Week ended:	Raised	Redeemed	Net New Borrowing
Oct. 20 ..	—	25.0	– 25.0
,, 27 ..	—	25.0	– 25.0
Nov. 3 ..	—	—	—
,, 10 ..	—	25.0	– 25.0
,, 17 ..	—	25.0	– 25.0
,, 24 ..	—	—	—
Dec. 1 ..	—	—	—
,, 8 ..	—	2.0	– 2.0
,, 15 ..	—	—	—
,, 31 ..	—	4.0	– 4.0
1952			
Jan. 5 ..	—	2.5	– 2.5
,, 12 ..	—	36.0	– 36.0
,, 19 ..	—	—	—

Britain's Gold and Dollar Reserves

(Millions of U.S. dollars)

Years and Quarters	Net Deficit	Financed by: U.S. and Canadian Credits	Purchases from I.M.F.	S. African Gold Loan	E.R.P.	Change in Reserves	Reserves at end of Period
1946	908	1123	—	—	—	+ 220	2696
1947	4131	3273	240	—	—	– 618	2079
1948	1710	352	128	325	682	– 223	1856
1949	1532	116	52	—	1196	– 168	1688
1950:							
I	+. 40	27	—	—	229	+ 296	1984
II	+180	18	—	—	240	+ 438	2422
III	+187	—	—	—	147	+ 334	2756
IV	+398	—	—	—	146	+ 544	3300
Total, 1950 ..	+805	45	—	—	762	+1612	3300
1951:							
I	+360	—	—	—	98	+ 458	3758
II	+ 54	—	—	—	55	+ 109	3867
III	– 638	—	—	—	40	– 598	3269
IV	– 940	—	—	—	6	– 934	2335
Total, 1951 ..	– 1164	—	—	—	199	– 965	2335

BARCLAYS BANK

RECORD GROUP FIGURES

FAILURE OF PLANNING

MR. A. W. TUKE'S REVIEW

THE annual general meeting of Barclays Bank Limited will be held on February 8 in London.

The following are extracts from the statement of the chairman (Mr. A. W. Tuke) circulated with the report and accounts for the year 1951:—

Our current, deposit, and other accounts at £1,284,691,537 show a small decrease on last year's figures. Advances show another substantial increase. The profit for the year is about £60,000 less; it has enabled us to recommend the usual dividends, and with the help of a draft on the "carry-forward" to set aside £1,000,000, compared with £750,000 last year. On this occasion the whole amount is being carried to contingency account.

In the consolidated balance-sheet the aggregate of the current deposit, and other accounts of the group at £1,818,231,403 is higher than ever before and reflects in particular a large increase in the figures of Barclays Bank (Dominion, Colonial, and Overseas).

Since our meeting last year the outstanding event in the affairs of the bank has been the withdrawal from the chairmanship of Sir William Goodenough in February last owing to ill-health, which was followed three months later by his untimely death. Measured by length of days, his life has indeed been a short one. Measured by its achievement he may truly be said to have rendered a full lifetime of service to the bank and to the community.

AN EXPERIMENT

During the post-war period the country has been subjected to an experiment in planning. The initial period of this experiment is clearly at an end, but no one knows when it may be renewed, and meanwhile we have an opportunity of standing back from the picture and seeing how it looks. Not all of us expected a masterpiece, but even the most optimistic partisans must be a little disillusioned by what they see at the present moment.

At this stage I may be told that I am treading on dangerous ground; that I am infringing one of the articles of the banker's faith, that he should at all costs avoid becoming involved in party politics. I fully acknowledge the validity of this doctrine at the time when it was enunciated and also at the much later date when I was taught it by my father, himself a private banker in his early days. Indeed, I should still regard it as most undesirable, so far as I personally am concerned, that I should take an active part in the affairs of any political party. But times change and we may have to change with them.

In olden days when the choice was between Whig and Tory, it mattered little to the banker which party was for the moment in power: indeed, the banker might possibly, as a Free Trader, favour privately the policies of the progressive party, and if he failed to observe the reticence enjoined upon him, it might well have been "the squire and his relations" who would have been scandalized. But in the process of political evolution, which has proceeded more and more rapidly during this twentieth century, we have arrived at a stage when an entirely new economic policy has been put to the test by the progressive party of the day. In these circumstances, if a business man, who is required or at least allowed by custom once a year to make public comment on the affairs of the nation, feels that the results of this policy have been and are likely to be disastrous not only to private enterprise, to which he pins his faith, but also to the true interests of the whole nation, from which all else depends, then it is surely his duty, even though he be a banker, to give expression to his views to the best of his ability.

Certain forms of State intervention in our economic life are inevitable, but I have no belief in the efficacy of any central control of all the manifold wants of fifty million people by means of a mass of permits, coupons, and licences. I am convinced that in these matters it is better for authority to confine itself to avoiding the creation of conditions in which it pays a man to break the law.

POST-WAR PROBLEMS

Towards the end of the second war responsible people in this country began to turn their attention to a consideration of the problems likely to arise after the end of the fighting. The available manpower, it was recognized, would be insufficient to satisfy the total demand for goods and services and some time was likely to elapse before the need would arise to put into operation any long-term policy for averting mass unemployment by stimulating demand.

Despite this, after 1945, the new Government instead of keeping the stimulant in reserve in case the patient should show signs of collapse, plied him with successive doses of alcohol when he was already slightly intoxicated. Realizing, however, that he could not be allowed out and about in that condition, they called in the planners to set up an elaborate system of controls with which to check, thwart and generally infuriate the unfortunate victim. And then they gave him another glass of champagne.

ANTI-INFLATIONARY STEPS

Attempts have been made, though until recently within narrowly restricted limits, to bring this inflation to a halt, and in this connection the extra expense of rearmament is a most disturbing factor, but until the last few weeks it seems to have been hardly realized that, whereas the new technique may be properly applicable in a time of depression, the old orthodox remedies may still be appropriate when inflation is rampant. There has been a heavy price to pay for this ever-increasing inflation and no one can say that there will not one day be an awful reckoning to be met, but for six years the fear of unemployment, which was a nightmare to many in the inter-war period, has been virtually removed, and there is no denying the comfort and reassurance that the existence of a sellers' market for labour has brought to many homes. But as a general principle neither the seller nor the buyer ought to have the whip hand in commerce. The ideal of permanent equilibrium is doubtless unattainable, and when thinking of buyers' and sellers' markets we should not forget that each one of us is both a seller and a buyer; a seller of the fruits of his own labour, and a buyer of the fruits of the labour of others. In present conditions a man finds it comparatively easy to earn a high wage but very difficult to buy with it the goods and services that he requires. It would be even worse to go to the other extreme, but he would almost certainly be better off if he had rather less money to spend but goods were more plentiful and therefore cheaper.

In retrospect one cannot imagine a more opportune period than the years since 1945 for the application of monetary discipline, and I have great hope that its adoption at the eleventh hour may yet put our economy on a sound basis. An expansionist policy, if under proper control, may well be the answer to the problem of mass unemployment in this country; that, however, does not justify its adoption in circumstances to which it was inappropriate.

RESULTS OF NATIONALIZATION

The railways provide a good opportunity for the public to weigh in the balance the fruits of the nationalization of an existing industry. In the past, although the service was by no means perfect, a reasonably high degree of efficiency was maintained in spite of restrictive legislation. When the railways were nationalized an immediate eruption of paint on the engines led one to hope that the service would perhaps be smartened up in other ways also, but this hope has proved groundless.

Another form in which the State has entered into business on a large scale in recent years is by means of the setting up of agricultural organizations of various kinds in undeveloped parts of the Empire. The conception of these projects was meritorious, but the fact remains that major failures and only minor successes have emerged.

Private enterprise would, of course, have proceeded quite differently, testing its theories by means of one or more small pilot schemes, and would probably have been content to wait ten years for a return on its investment, but private enterprise does not bear the responsibility for feeding the nation.

Perhaps the lesson to be learned from these unhappy experiences is that pioneering is inevitably a very slow job and that the method adopted by private enterprise is not easily improved upon by the most carefully laid plans, even when the planning is backed by the almost unlimited financial resources of the State. In one way or another probably £50m. of the taxpayers' money has been wasted, or I will say spent, in learning this lesson. It seems reasonable to assume that if wastage of this kind affects business enterprises run by the State it must also permeate the whole field of Government expenditure. That is where the pruning knife should be applied.

HOMES FOR THE PEOPLE

Perhaps the most important of all the nation's internal activities since the war has been the effort to provide homes for the people. I feel certain that the insistence of the late Government on retaining this activity so largely in public hands has caused quite needless inflation of the price of new houses. I believe that, if private enterprise had been allowed to operate freely in this field, subject only to control of design and construction and to a ceiling price, the result, given the co-operation of the trade unions concerned, would have been a lowering of the cost of the finished article.

I am very glad to see that the new Government has decided to encourage home ownership and that the local authorities may now, subject to conditions, sell individual houses to those of their tenants who are able and willing to buy them. Every pound that is repaid to the Government by this means will enable it to wipe out a pound of inflationary debt, just as every pound that has been borrowed by the Government in recent years to finance local authorities for this and other purposes has increased the inflationary pressure.

THE HUMAN FACTOR

Instances of the failure of nationalization and other planning activities to achieve what their protagonists expected of them could be multiplied. Even in the coal mines, where it was generally conceded that some major change was necessary, the results are most disappointing.

Is there some constant factor in all these plans which causes such unrelieved failure? They are, I am sure, prepared with the greatest care by men of outstanding ability and of the highest intellectual integrity, but unhappily the cleverest men often seem to be somewhat lacking in common sense and worldly wisdom. They do not and cannot make allowance for the reactions to be expected from human beings and from the forces of nature, which will beat them every time.

BARCLAYS BANK LIMITED

Anthony William Tuke, *Chairman.*
Frederick Cecil Ellerton, *Deputy Chairman.*
Cuthbert Fitzherbert,
Anthony Charles Barnes, D.S.O., O.B.E., *Vice-Chairmen.*

General Managers:
G. F. Lewis, R. G. Thornton, J. D. Cowen, E. Brimelow.

Statement of Accounts, 31st December, 1951

LIABILITIES

	£
Current, Deposit and other Accounts	1,284,691,537
Acceptances, Guarantees, Indemnities, etc., for account of customers	64,207,500
Paid-up Capital	15,858,217
Reserve Fund	13,750,000

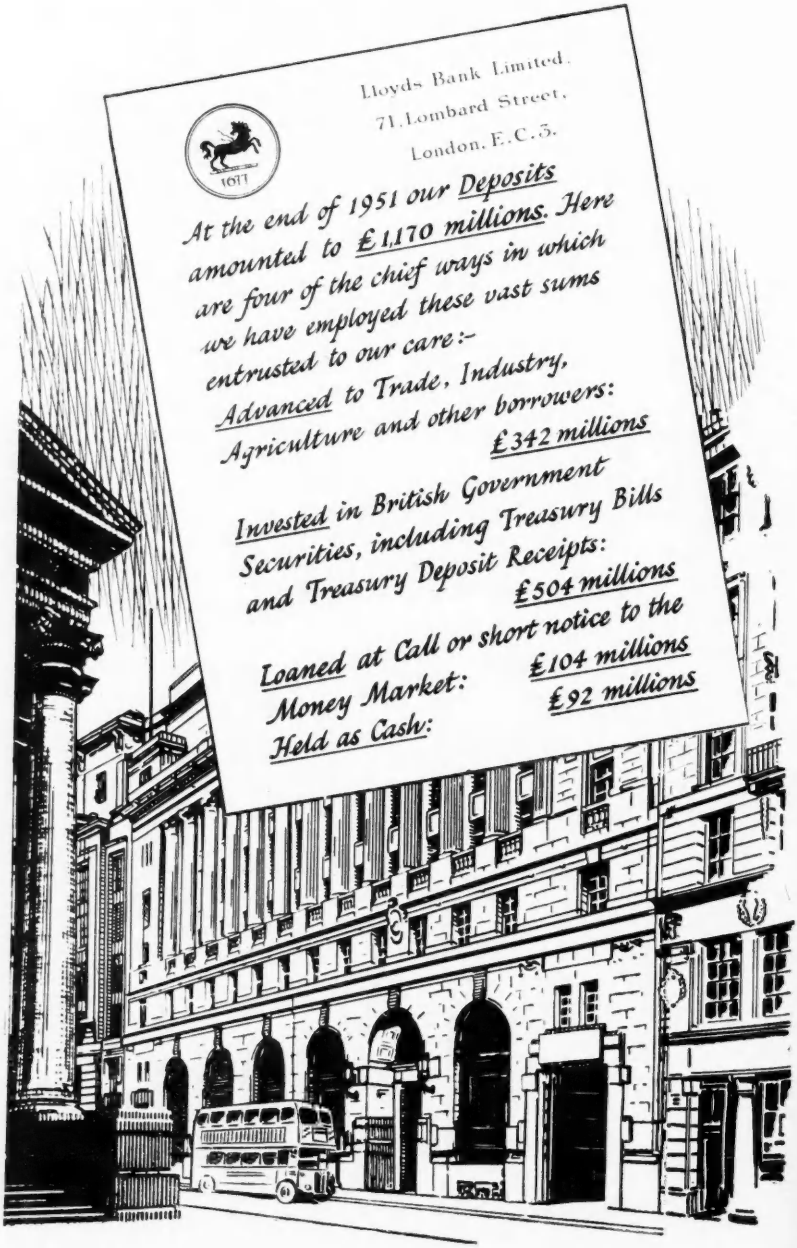
ASSETS

Cash in hand and with the Bank of England	107,663,234
Balances with other British Banks and Cheques in course of collection	52,125,546
Money at Call and Short Notice	89,481,000
Bills Discounted	237,686,175
Treasury Deposit Receipts	22,000,000
Investments	415,244,694
Advances to customers and other Accounts	367,157,760
Investments in Subsidiaries :—	
The British Linen Bank	3,728,558
Other Subsidiaries	9,058,778
Other Trade Investments	1,588,670
Bank Premises and adjoining Properties	8,565,339
Customers' Liability for Acceptances, Guarantees, Indemnities, etc.	64,207,500

HEAD OFFICE :

54 LOMBARD STREET, LONDON, E.C.3

An Account of Stewardship


Lloyds Bank Limited.
71, Lombard Street,
London, E.C.3.
1677
At the end of 1951 our Deposits amounted to £1,170 millions. Here are four of the chief ways in which we have employed these vast sums entrusted to our care:-
Advanced to Trade, Industry, Agriculture and other borrowers: £342 millions
Invested in British Government Securities, including Treasury Bills and Treasury Deposit Receipts: £504 millions
Loaned at Call or short notice to the Money Market: £104 millions
Held as Cash: £92 millions

LLOYDS BANK LIMITED

THE INFLATION DANGER

LORD BALFOUR OF BURLEIGH'S VIEWS

THE annual meeting of Lloyds Bank Limited will be held in London on February 15.

In the course of his statement accompanying the report and accounts for 1951, the chairman, the Right Hon. Lord Balfour of Burleigh, D.C.L., D.L., says:

Our profit at £1,815,858 is £54,255 higher than last year and may be considered satisfactory in view of the continued increase in running expenses. It will be realised, however, that we have not been able to provide for the depreciation of our investments out of the profits of the year, but have utilised a part of our internal reserves for that purpose.

Instead of allocating any of our profits to our published Reserve, we have on this occasion utilised the whole of our profits in excess of the amount required to meet the dividends for the purpose of strengthening our internal reserves.

Our investment reserve, buttressed by transfers from less immediately needed reserves, has taken care of the whole of the depreciation without unduly depleting our contingency reserve. The history of the last three months illustrates forcefully the need for powerful internal reserves and justifies the prudent policy we have always followed.

BALANCE-SHEET FIGURES

Referring to the balance sheet, our Current, Deposit and Other Accounts at £1,171 millions show a comparatively small increase of £22 millions over last year.

The principal changes in our figures will be found on the Assets side of the balance sheet. The effect of the Government's operation in the funding of a portion of the floating debt is shown in the fall of £62 millions to £156 millions in our holding of Treasury Bills and an increase of £87 millions to £329 millions in the figure of British Government securities. There has also been a welcome fall of £65 millions in our holding of Treasury Deposit Receipts.

Loans and Advances at £342 millions show a further increase of £53 millions and with the present high prices ruling and the necessity for assisting industry engaged on rearmament work, the export trade and agriculture, it is difficult to visualise any immediate fall in our Advances in spite of our determination to reduce the supply of credit for less essential purposes.

Our business in India and Pakistan continues to make satisfactory progress, the rise in raw material prices having been reflected in an increased demand for banking accommodation.

OUR LIVELIHOOD IN DANGER

Our national standard of living, our daily bread, is in more acute danger than ever before in our long history, whether in peace or war. Unless we can learn to pay our way abroad, then, as Mr. Butler very truly said, we shall before long find ourselves "bankrupt, idle and hungry." Views may differ about the steps which must be taken to ward off that very real threat; what is important, as Mr. Gaitskell urged last October, is that arguments should be appraised on their own merits, that we should argue it out "peacefully, fully and if possible rationally and calmly."

To the ordinary citizen, the crisis in our overseas payments may well appear to have come upon us out of a clear sky. That is not so.

Even 12 months ago, therefore, the situation was already one of great danger. For if there is one lesson of economic experience which admits of no dispute, it is that a country in which inflation is rampant will always experience the greatest difficulty in balancing its overseas payments.

While I am confident that the measures now being taken are precisely what is needed to put us on our feet again, time is needed to achieve results, and meanwhile our reserves have already been brought very low.

Two facts will have emerged clearly, I trust, from this brief survey of the nature and origins of the crisis. First, that when the new Government assumed office they were confronted with a situation which if not desperate was desperately critical. Secondly, that this critical state of affairs cannot be cured unless domestic inflation is checked.

RETURN TO MONETARY DISCIPLINE

In one respect, however, the remedial measures adopted do differ from those employed on previous occasions—and it is fundamental. I refer to the decision to reinforce the physical controls by the use of monetary measures. This is the most important change in our official policies for many years past and holds out the first real hope of escape from the inflationary quagmire in which we have been floundering since the end of the war.

For some time past the rate of expansion in bank deposits has been very small. Nevertheless, there has at all times been more than enough money in existence to feed the inflation; what we have needed has been an actual reduction in the volume of deposits.

DEPOSITS AND CASH RATIO

But, it will be objected, the volume of bank deposits is rigidly linked, by the maintenance of an 8 per cent. cash ratio, to the amount of bank cash reserves. If the authorities were anxious to keep down the volume of deposits, could they not easily have done this at any time simply by refusing to make available the additional cash needed to carry any additional deposits? That is indeed so. But the adoption of this method was ruled out, until the recent

change of policy, by the determination to prevent any rise in the Treasury bill rate from the exceptionally low level of around ½ per cent. at which it had been pegged.

To end this system by which the Treasury bill rate was pegged at ½ per cent. was thus the first indispensable step towards the resumption of control by the authorities over the supply of bank cash, and therefore of control over the volume of bank deposits.

OBJECTIVES OF THE NEW POLICY

The intention of the authorities is, by keeping a tight rein on the supply of money, to reduce spending. Hitherto, though many sections of the community have been feeling the pinch of higher prices, the nation as a whole has had money to burn; henceforth, in this as in more literal respects, there will be a shortage of fuel.

How far must this restraint of spending be carried? The basic rule is that it is one man's spending which creates another man's income. The object, clearly, is so to restrain expenditure that incomes as a whole at least cease to expand, except as the counterpart of increases in output. There is no question of seeking abruptly to bring down prices by cuts in wages or the deliberate creation of mass unemployment. Once an inflation has taken place it is almost impossible to put the clock back; deflation carried to extreme lengths can be as great an evil as inflation and, like inflation, can give rise to much social injustice and hardship.

INCREASED PRODUCTIVITY THE SOLUTION

If the cost of living is to be brought down again, the reduction must come from other factors than cuts in money earnings. A fall in import prices would help, but it would clearly be unwise to count on this in the immediate future. The real solution must be an all-round increase in productivity. Nobody could contend that in the hot-house atmosphere of inflation our labour force has either been distributed to the best advantage between industries or has been working flat out. Now the windows are open again and the invigorating effect may work wonders.

All this may seem very remote from specific problems of great urgency, such as the need for more coal, the need to fill the half a million or more vacant jobs in defence industry, to curb imports and step up exports. In reality, it has the closest possible bearing on all such matters. To halt inflation admittedly will not solve all our problems overnight, but it is the first indispensable step and may well open up the way to a solution of problems that have seemed literally insoluble so long as inflation has persisted.

If the inflation is halted, the community as a whole will find itself in the position of a prudent housewife deciding how best to spend a strictly limited family income. If the prices of essentials rise, she is left with less to spend on non-essentials and must buy less of them. Once inflation is halted we need no longer fear a wages spiral. There need be no inhibitions about granting higher wages in the industries to which it is sought to attract workers.

Given an end to inflation the people will no longer have the money to spend on the products of the less essential industries. Profits, turnover and employment in those industries will contract, as it is desirable in the national interest that they should. Workers will be released to make their way to the expanding defence and export industries. And with half a million or more vacancies to be filled in the essential sector there can be no danger that the contraction elsewhere will give rise to any lasting unemployment. I recognise that even transitional unemployment means hardship for the individuals concerned, but the alternative—if the necessary redistribution of labour is not effected—is mass unemployment due to inability to buy raw materials.

By thus loosening the rigidities of our economy, the halting of inflation will help at the same time towards the supreme objective, which is to rectify our balance of payments. Indeed, the elimination of excessive monetary demand will assist in a number of ways. We have already seen that the untimely increase in the volume of imports during 1951 was due at least in part to the fact that home consumption was rising when it should have been falling. The inflated home demand for goods and services must also have been a factor impeding the expansion of exports. A slackening in home demand will not enable us to sell goods abroad if the markets for them do not exist or if we are unable to meet the challenge of reviving Japanese and German competition; but it will at least release goods for our exporters to try to sell abroad.

STIMULUS TO SAVINGS

These, then, are some of the reasons why I believe the determination to set to work once again our rusty and forgotten monetary machine to have been a decisive turning-point. They are by no means the whole story. I have concentrated on one simple aspect of the question: the fact that if incomes are limited higher prices in one direction mean less spending in other directions, and some of the beneficial consequences that flow from that fact. But in this sphere above all nothing succeeds like success. When prices are rising, this very fact makes people less willing to save, more anxious to spend—whether on the purchase of a new hat or the building of a new factory—before prices rise against them. Inflation feeds on itself. In the same way, the halting of inflation can transform the whole atmosphere.

We must all play our part, uncomfortable though it may be, in keeping prices under control, and this is where the collaboration of the T.U.C. may be decisive. That great organisation will, I am certain, use every means in its power to bring home to its members what runaway inflation means. Inflation must be halted. The process will be painful—it has already proved so to the banks, who have suffered tens of millions of depreciation in the market value of their gilt-edged investments. But for the countless victims of inflation—the millions whose incomes have not kept pace with mounting prices—the return to some degree of monetary discipline holds out the first real hope of a tolerable future.

MIDLAND BANK LIMITED

DETERIORATION IN NATION'S ECONOMIC HEALTH

URGENCY OF REMEDIAL ACTION NECESSITATES ALL-ROUND CO-OPERATION

ILLUSIONS CREATED OR FOSTERED BY INFLATION

STATEMENT BY THE LATE CHAIRMAN

THE one hundred and sixteenth annual general meeting of Midland Bank, Ltd., will be held on February 15 at the head office, Poultry, London, E.C.

The directors deeply regret the loss, by sudden death, of their distinguished Chairman, The Most Hon. The Marquess of Linlithgow. In the circumstances they feel it would accord with the wishes of the shareholders that his statement, which was at an advanced stage of preparation at the time of his death, should be circulated without amendment. Extracts therefrom follow.

In my statement a year ago I noted the progress which seemed to have been made, on the test of generally accepted data, towards equilibrium on the balance of payments of the United Kingdom and the sterling area as a whole; at the same time, however, I suggested that the prime cause of anxiety for the immediate future was to be seen in the continuance, and perhaps intensification, of inflationary pressure within the national economy. The close connection between these two elements in the situation has been abundantly demonstrated in the course of events over the past year. Inflationary pressure has found expression in an accelerated shrinkage of the domestic purchasing power of the pound, while a dramatic change has manifested itself in the international position of sterling. The balance of payments of the United Kingdom, and indeed of the entire sterling area, has undergone a sharp deterioration; the steady building up of gold and dollar reserves was succeeded by an alarming drain, accompanied by a reversal of the creditor position earlier established in the operations of the European Payments Union.

It is a difficult time at which to comment constructively on such a manifestation of weakness. Various measures aimed at arresting the deterioration and strengthening the bases of recovery are being applied, and until a more comprehensive plan of action has been worked out than could have been elaborated at this stage it would be premature to pass judgment and something less than helpful to press detailed proposals. What can perhaps be done, by way of constructive assistance to those responsible for shaping policy and action, is to make some contribution towards a wider understanding of the nature of the difficulties that must be overcome before economic health can be fully restored. No one, surely, can be so complacent as to suppose that such a task is redundant or that the educative process has been completed by the impact of the series of economic "crises" experienced since the end of the war.

THE SETBACK OF 1951

The record of 1951 is a disappointing setback to the high hopes that had been engendered by a period of comparative steadiness and reinforcement, supported by American aid and fostered by the opportunities in export trade afforded through devaluation and an expansion of world demand. To some extent the brighter prospects were frustrated by the added strain put upon the economic system by growing international political tension. The resultant pronounced rise in world prices of many primary commodities served to enlarge the gold and dollar resources of the sterling area; on the other hand, it combined with the secondary effects of devaluation to bring about a marked increase in the cost of many raw materials used in British industry; and the

all-round levering up of industrial costs has only latterly been slightly relieved by some decline in primary prices from the peak of the upward movement. The necessity of swift rearmament within a concerted plan of Western defence has imposed upon our productive capacity a requirement the magnitude of which has perhaps scarcely yet been generally appreciated. With that superimposed requirement, however, it has become clearer than ever before that we in this country have been living under a condition of continuous overstrain of economic resources. The quickened depreciation of the pound and the violent disturbance of the balance of payments are correctly to be regarded as more than ordinarily conspicuous and convincing evidence of a long-standing condition. The new demand upon the national resources tipped the scales, in an unsteady balance, so that the weight of excessive demand made itself apparent in unmistakable terms.

I tried to show last year that the prospective rearmament demand would call for a substantial diversion of growing productive resources, and suggested that it ought to be brought about primarily at the expense of current consumption. The records show that in fact this redirection of productive effort did not take place in the smooth and orderly manner that might have been hoped for—indeed, the volume of consumption seems to have been maintained in 1951 at the previous year's level—and the failure must be attributed, on the evidence, to the continued inflexibility of our economic system. In an economy like ours, peculiarly bound up with international trade and therefore sensitive to abrupt changes in world conditions, a high degree of adaptability is required; and this is all the more necessary when, as throughout the post-war period, productive capacity is fully engaged, with little or no slack to be taken up in response to a sudden expansion of a particular element of demand. Even before rearmament became an important factor, there had been continuing pressure to take more out of the national product in consumption, on governmental and private account together, than would allow for all the capital reconstruction and improvement that might have been justified under other conditions. The rearmament programme introduced a new competing demand which involved considerable recasting of the pattern of production as well as substantial diversion of the product of industry away from consumption or capital construction. The required adaptation was not forthcoming.

Apart altogether from familiar price indices and figures of gold reserves and balance of payments estimates, evidence of this lack of adaptability is to be found in a variety of forms. It can be seen, for one thing, in the excessive demand for some kinds of labour, contrasted with a shortfall in other branches of industry. There are reported to be several hundreds of thousands of unfilled vacancies listed at employment exchanges, arising largely in undertakings directly or indirectly concerned in defence contracts, while it is understood that workers are being retained in some places in excess of current requirements for fear of inability to recruit when restored supplies of raw materials, re-expansion of consumer demand or other factors make full running possible again. In contrast, many thousands of employees elsewhere are working short time, some because of a shrinkage of current demand for their products, others because of an irregular flow of materials. Clearly, skilled workers cannot be switched freely and swiftly from one kind of process to a totally different occupation; but there seems to have developed too close an adhesion of the particular man to the particular job—a degree of rigidity in the supply of labour which is traceable to many factors, including housing difficulties and travel problems, as well as direct inducements embodied in individual terms of employment. Further evidence of strain is to be seen in a reversion in some trades to lengthening delivery dates and renewed difficulty in accepting orders for export markets. Irregularity in the supply of materials, not to mention fuel and power, and immobility of labour are incontrovertible evidence of the sustained pull of excessive demand on limited, though still growing, productive capacity.

Symptoms of strain are to be seen also on the financial side of affairs. Year by year, the budget has been so framed as to exert a counter-inflationary effect by withdrawing monetary resources from consumers and those who might otherwise set up undue demands for capital goods; but every addition to the burden of taxation has entrenched further upon the ability and willingness of the individual to maintain his personal savings, and has thus to a large extent defeated its own purpose. The incomplete effectiveness of counter-inflationary budgets—given an already high level of taxation—has been reflected in the reappearance of the spiral of costs and prices. In the first eleven months of 1951 nearly twelve million workers were affected by rises in wage rates, computed to have added roughly seven per cent. to the national wages bill, and these are far larger aggregates than in any preceding year. Similarly, the rise in the index number of retail prices has been more pronounced than over any equal period since the end of the war.

REMEDIAL MEASURES

It would be absurd to look for a single remedy for overstrain and rigidity resulting from this complex of factors. Direct curtailment of public and private capital construction has been resorted to more than once already, as has direct restriction of imports, and no one supposes that these alone will this time be more lastingly effective than in the past. There is room for fiscal measures, though at this stage probably only by re-allocating the burden so as to increase the incentives to work and resourcefulness, rather than by aiming at a more powerful impact on spending power as a whole. Relief, too, may be found by economies in current Government expenditure. Financial

controls, especially over borrowing for capital and other transactions, have again been tightened in pursuance of the general purpose; and the new monetary conditions, referred to in more detail in later paragraphs, may be expected, through their effect upon the lending powers of the banks, to deflect some of the less urgent demands upon the nation's productive capacity. Beyond all these measures, however, is the need—progressively insistent for many years stretching back into pre-war times—for greater elasticity in the economic system as a whole and the requirement, which has characterised more particularly the post-war phase, of a general slackening of tension throughout the productive and trading organism.

Government measures, however wisely conceived and judiciously applied, cannot alone bring about this restoration of the quality of responsiveness and adaptability. Complete and speedy success, bringing its benefits to all sections of an inter-dependent community, requires the full co-operation of all—co-operation springing from conviction as to the nature of the requirements and the urgency of remedial action. Whatever Government may be holding office for the time being, it must for this purpose be able to count upon enlightened support for a plainly expounded policy, fair in its incidence and designed to serve the national interest as a whole. On this account encouragement is to be derived from the statesmanlike declaration by the General Council of the T.U.C. of its readiness to co-operate with the new Government in finding " practical solutions to the social and economic problems facing this country " and to advocate policies which it " believes to be in the best interests of the country as a whole." Nowhere is general understanding of the basic issues more necessary than in relation to monetary policy, and perhaps the most useful groundwork that can be done in this field is to identify and expose in the plainest possible terms some of the illusions created or fostered by inflation. They seem to me to group themselves conveniently under four headings.

ILLUSIONS FOSTERED BY INFLATION

The first may be called the illusion of welfare, which springs from the fact that inflation is usually accompanied by over-full employment with rising incomes—incomes swollen not only by successive increases in wage rates, but also by a variety of incentive payments and amenities and by opportunities of work at overtime or other special rates. Too often it is forgotten that the inevitable concomitant of inflation is a cumulative rise in prices, including even the basic and subsidised living costs. There is a tendency, moreover, to overlook the growing number of cases of hardship that arise where incomes are relatively, or indeed quite, unresponsive to a rise in the cost of living. Yet another incident of the general process is that the burden of taxation tends to grow, if only because of the diminution of the real value of income-tax allowances and the movement of increasing incomes into the range of high tax rates. Thus inflation accounts for the fact that, despite successive post-war Budget reliefs for smaller incomes, the number of people paying income-tax to-day is larger than ever before. Taking all things together, then, it is justifiable to say that the nominal enlargement of welfare is to some extent illusory. To illustrate the danger of the illusion, which became apparent in the history of not a few countries after the first world war, it would be possible to have in the United Kingdom several tens of millions of millionaires; but it would be a country well on the way to ruin, and many of its citizens, though millionaires, would already have been ruined.

Secondly, there is the illusion of security. The loss of value of accumulated savings, through long-continued inflation, has latterly become widely appreciated and may indeed have been a deterrent to fresh saving out of current incomes, thus giving added impetus to the inflationary trend. Less widely apprehended are the similar effects upon the adequacy of personal provision against misfortune, as through life insurance and contributory schemes for the protection of widows and orphans. All such arrangements presuppose a more or less stable value of money, and the momentary satisfaction to be derived from a growing income in terms of money is all too little to set against the risk that provision for dependants which seemed adequate when the arrangements were made should turn out to be so deficient, when the need arises, as to condemn them to uncovenanted hardship. The same observation would apply to pension schemes under which some part of an individual's immediate spending power is forgone for the sake of an income in old age which may turn out to be far smaller in terms of necessary goods and services than he had been entitled to expect. Closely related to such private frustrations are the inroads made by inflation upon social service provisions, exemplified by the severe cut in the value of the family allowance since the payment of five shillings a week for each child after the first was enacted by Parliament in 1945.

A third count in the indictment of inflation is on the ground that it creates an illusion of greater progress than is in fact being achieved. This is well illustrated by the tendency to treat a rise in such figures as the total of bank deposits or the turnover of trade as measures of business expansion when they may reflect nothing more than a rising level of prices and costs. Under similar conditions a growth of national income is deceptive until the figures are adjusted on to a common price basis, while the amounts applied out of current income to the improvement of economic and social capital may likewise be overstated. Compilers and interpreters of such statistics for public information find it a hard task to present the figures in a way that will defeat their inevitable tendency to deceive, and almost impossible to guard against the ever-present risk that less skilled commentators may be also less scrupu-

lous to present the statistics with all necessary qualifications It is so much easier to take the figures at their face value.

Closely allied with the illusions of welfare, security and progress is the illusion of prosperity. In times of inflation business profits, as ordinarily computed, show an expansive trend, and Government revenue from the taxation of profits is correspondingly buoyant. But just because profits are easier to make than in more rigorous times the incentives to economical production and distribution are weakened. In reality, the profits themselves are largely illusory. The generally accepted system of accountancy, sanctioned by law and by tax practice, presumes a stable monetary unit, having the same value over a long period and for all business purposes. When, as happens in an inflationary period, various items of running costs and revenues, liabilities and assets are reckoned in units of different value the upshot of the whole accounting exercise is falsified. As is now becoming clear to business men, if not to the public generally, growing nominal profits have come to represent in part the " gain " resulting from the rise in values of stocks of goods—which will have to be replaced, when sold, at the higher level of prices—and from applying to the replacement of fixed assets a depreciation allowance which will go only part of the way to finance replacement at a much heavier monetary cost. In such circumstances a wise business management will set aside, to additional reserves, a large part of the accounting " profits ", but the illusion has already been created by the anouncement of increased profits, and tax has already been levied on this fortuitously swollen figure. Thus some part of the tax on profits—and perhaps even some part of the dividend paid out—may in effect have been levied on the capital in the business, while true profits, so far from increasing, may in reality have been shrinking.

THE PROCESS OF INFLATION

Where, then, lies the source of these illusions, so far as they have become current in our own country? It seems to me that the answer can be put most clearly in the form of symbols. During a given period the productive resources of the country can be expected to pour out goods and services the value of which may be called x, in millions of pounds reckoned at the prices ruling at the outset of the period. Much of this total output—call the amount a—will be used up in personal consumption, in the form of food and drink, clothing and shelter, recreation and so forth; while some of it, say b, will be similarly used by the Government, as for feeding, clothing and equipping the Armed Forces. Over and above current consumption, both Government bodies and private undertakings and individuals will be adding to or improving capital equipment, by building houses, schools and factories and installing new machinery. These items we may call c and d. Under conditions of monetary stability and in a flexibly working economy, $a+b+c+d$ will just about equal x; but, in fact, we know that the calls made under these four headings have together persistently tended to outstrip x, and this means that not all the demands on x could be met. Now comes a large and insistent demand for rearmament, to be designated e. If, then, it turns out that all these demands together, as they are exercised, substantially exceed x, then the equation can be established in only two ways or a combination of them. The difference may be made good by supplementing x, that is, current production, by various means—by drawing upon accumulated stocks of goods, by using up overseas capital or gold reserves to pay for added imports, or by obtaining gifts or loans from other countries. And if all these together should prove insufficient to bridge the gap, then the only way equilibrium can be brought about is by the upvaluing of the multifarious items of goods and services that go to make up x—that is, by an all-round rise in prices and costs. In practice the train of adjustment is continuous, affecting all items in the equation; the various elements of demand tug incessantly at the supply of goods and services, stretching it continuously and competing against each other in an endless process of revaluation. The danger is that the process should tend to gather speed under its own momentum.

The sequence I have tried to depict is, broadly, a true-to-life record of what has been happening in this country, very clearly in the past year or more but on a more moderate scale ever since the end of the war. One of the two major means of adjustment of the equation is simply described as a recurrent deficit on the balance of international payments and earnings; the other is the continuous reduction of the purchasing power of the pound. Both are evidence of a persistent attempt to do more, by way of consumption, capital construction and defence, than our current productive resources and effort would justify—an attempt, that is, to live beyond our means. We need, however, to note that productive resources can be overstrained either—or both—because the demands made upon them are too large or too highly concentrated at particular points, or because the resources are not deployed in the best possible way. From this it follows that a relaxation of the strain does not necessarily call for a ruthless curtailment of demand; it may be brought about largely or wholly by a better use of available resources, or, in the accepted phrase, by higher productivity if within this term be included the provision of basic services essential to a regular flow of raw materials and components throughout industry and, in addition, a ready adaptability to changes in the composition of demand. Thus we are brought back to the fundamental need of a change in the whole bodily condition of our economic organism.

CORRECTIVE POLICY

It was no doubt with this need in mind that the Chancellor of the Exchequer, when an-

nouncing changes in monetary arrangements early in November, spoke of the necessity of "producing the right financial climate" in order that the Government's "intention to make and keep sterling strong" should be carried out. It was reassuring to note in the same statement clear recognition of the fact that drastic, unregulated deflation is no proper corrective for inflation. True, it reverses the trend of monetary conditions; but experience between the two wars, here and elsewhere, showed that it creates as many grave difficulties, multiple frictions and gross inequities as it can ever remove by the arresting of inflation. Too often the attempt has been made to go back in our tracks—with disastrous results. I am not sure that the use of the word "disinflation" as something readily to be distinguished from "deflation" is helpful to an understanding of what is required; but there is sound reasoning in the attempt to bring about the removal of the inflationary element of demand, so as to achieve a steady equilibrium in the monetary system, while avoiding resort to indiscriminate and ruthless monetary deflation. The one course of action, recognising that much of what is done cannot be undone, is designed to arrest the inflationary process and re-establish a firm foundation for the future advancement of the general welfare; the other creates a whole new set of violent disturbances and distortions, and thereby further postpones the establishment of a healthy basis for a sustained high level of economic activity. Uncontrolled deflation ignores the dividing-line between full employment and serious underemployment; what is called disinflation—or, with due regard for the significance of the adjective, controlled deflation—if skilfully managed, is carefully regulated with close and continuous regard for the dividing-line between over-full and full employment, between debilitating strain and continuous, healthy activity.

Monetary action of this sort, however, cannot safely be charged with the entire responsibility for restoring health to our economic system. As already indicated, it has properly to be regarded as one part of a general aasault on rigidity and inflexibility throughout the economic system. There lies the main guiding principle for action. If it could be generally accepted, as the logical outcome of intelligent understanding of the nature of our ills, then those responsible for directing the course of national affairs and setting the tone of business policies would be well on the way to restoring vigorous, lasting health to the economic system. Without general agreement on guiding principles—or if public attention should be distracted by non-essential differences—the ultimate restoration of economic health can come about only by way of incalculable hardship, disruption and disaffection.

RECENT MONETARY MEASURES—EFFECTS ON THE BANKS

In fulfilment of the Government's "intention", as just quoted in the words of the Chancellor of the Exchequer, among the first measures announced was an attempt to bring about "a clear change of emphasis" in monetary conditions. It was made evident that the banks would have an important part to play in this reshaping of the financial background of public and private business, and their conception of the requirement thus placed upon them was plainly expressed in the "warning" and "appeal for co-operation" issued to the public through the Press at the end of November. While, to quote the Chancellor again, "any sharp attempt to try to switch to drastic deflation would be unwise", the aim is to establish conditions in which credit will be available only for essential purposes and only in the minimum amounts indispensable for such purposes. The changed position of the banks, with their liquidity sharply reduced by the funding of Treasury bills and with a closer hold by the authorities on the cash base, and the new official statement of the standards to be applied to the purposes for which bank credit should be made available are both directed to this end. The banks will be faced with many difficulties in carrying out this policy, but, as hitherto, can be relied upon to give the authorities their full co-operation in making the policy effective for the long-run benefit of the national economy. At the same time, the needs of essential production and trade can assuredly count upon receiving the most sympathetic consideration.

It is perhaps not surprising that critics of the Government's policy should have aimed their fire largely at the banks, notwithstanding their innocence of any part in shaping it and the fact that the banks had long been receiving an inadequate return from short-term Government borrowing. The particular presumption which is held to bring the banks properly under criticism is that the recent all-round rise in interest rates will yield them—so it is alleged—wholly unwarrantable enrichment at the expense of the taxpayer and, more especially, the borrowing customer. The wide dissemination of this allegation and its ease of repetition and acceptance make it necessary to give an objective reply.

NECESSARY FORTIFICATION OF FINANCIAL POSITION

The monthly returns of assets and liabilities of the London clearing banks provide a basis for an enlightening piece of arithmetic. From these figures anyone can deduce that the net addition to the annual gross revenues of the banks brought about directly through the officially actuated rise in rates on various bank assets—that is to say, on their holdings of bills and the new funding stocks, together with their short loans—offset by higher outgoings in deposit interest, probably works out at about £6m. before allowing for any continuance of the upward trend in costs of operation. Of this sum, however, the amount left at the disposal of the banks would be less than one-half,

the larger part being paid over to the Exchequer by way of profits tax and income-tax —to take no account of any possible further taxation of profits. As for the remaining few millions of pounds, it can by no means be considered as an addition to profits freely available, if the directorates of the banks were favourable to such a course, for distribution to shareholders in increased dividends—in which event, by the way, the share taken in taxation would be automatically increased. It is common knowledge that the investments held by the banks, notwithstanding the predominance among them of securities with fixed dates of redemption in the fairly near future, have undergone substantial depreciation by the test of market prices which govern their valuation for balance-sheet purposes. The clearing banks' investment holdings—practically all of them gilt-edged securities, and therefore comparatively low-yielding—even before the recent funding of Treasury bills amounted to more than £1 550m., and a decline of only one per cent. in average values between balance-sheet dates entails a loss far exceeding the net addition to the banks' revenue, as just computed, after taxation. If it be argued that this is no more than a book loss, unless the securities are in fact sold at market prices, the answer is that nevertheless the requirements of the Companies Act as applied by accepted accounting procedure make it necessary to write down the investments to market value where this is below the preceding balance-sheet valuation. In recent years this procedure has made heavy inroads on the " inner reserves " accumulated by the banks out of taxed profits. Quite apart from balance-sheet requirements, moreover, the tighter credit conditions foreshadowed by official action might conceivably enforce actual realisation of some bank investments, at market prices, in order to meet inescapable demands for credit for essential industry.

The simple exercise in arithmetic, the result of which I have just given, indicates that any likely addition, through higher interest rates, to the net income of the banks after taxation will go only a small part of the way to making good the entrenchments, due to writing-down of investments, on inner reserves that have been unavoidable in the long period of rising yields in the capital market. Ordinarily, that rising trend would have been reflected in an upward course of short-term rates, but in the post-war years these have been pegged at a low level. Accordingly, the banks have been deprived of the added revenue, from the more liquid assets, to compensate for the capital depreciation of investments. The recent addition to their revenue is a belated and necessary fortification of their financial position. Just as the Government's purpose, in its monetary policy, is " to make and keep sterling strong ", so it is in the interests of all that the banks of this country should maintain their record—perhaps unique in the history of our troubled times—of unquestioned stability and strength.

From the regular analysis of our own advances we find that the entire increase over the year is traceable to the requirements of industry, agriculture and trade, while lending to financial undertakings and to professional and private people has been held down to the figures of a year earlier. To judge from the details for the various sub-groups, the rise in business requirements has been necessitated by the all-round increase in costs of raw materials, fuel and power, labour and other necessities and the high level of activity, particularly in industries affected by defence orders.

For the immediate future, it is to be expected that the banks will find it more difficult than in the past to meet even these necessary demands. For one thing, to judge from the terms of the announcement, last November, of the change in monetary policy, it is no longer safe to assume that additions will be made to the cash basis to support any legitimate expansion of the volume of bank lending. Thus the more exacting selectivity called for by the new request addressed to the banks by the Treasury towards the end of the year may be reinforced by quantitative limitation of the banks' lending power.

EXPANDING VOLUME OF BUSINESS

The volume of business passing through the bank has remained on a steady upward trend, quite apart from the larger turnover due to higher costs and prices throughout the economic system. It reflects great credit on our administrative and managerial organisation and on the entire staff at head office and branches that this growing volume of business is handled so smoothly and efficiently and with the assurance to the public of unsurpassed safety and accuracy. Customers of the bank, I am sure, are fully appreciative, along with shareholders, of the inestimable value of skilled, reliable and courteous service, and to every member of our personnel sincere thanks are due and gladly forthcoming.

While the expansion has been general, one particular branch of our work may be mentioned for its interest in relation to current monetary developments. Activity in our overseas business has been maintained at the very high level which entitles us to claim pre-eminence in the financing of international trade through London. Not only does the volume of this business constitute in itself an important part of our bank's affairs, but through it we are enabled to provide a valued service to our customers in helping to solve the many problems which confront them in their foreign trade. This special service is facilitated by our widespread network of contacts with banks all over the world, contacts which are steadily cultivated by a two-way traffic of personal visits and also by the special arrangements we have developed in this country for the practical assistance of traders.

The Country's Business–and the Midland Bank

The Bank's balance sheet for December 31 last shows on one side nearly £1,350 millions of deposits, representing part of the circulating money used for the country's day-to-day business. On the other side appears £393 millions of advances, covering the needs of manufacturers, farmers, traders, professional and private persons for their essential purposes.

NATIONAL PROVINCIAL BANK

GOVERNMENT'S EFFORTS TO COMBAT INFLATION

THE EARL OF SELBORNE ON COUNTRY'S ECONOMIC PROBLEMS

THE 110th Annual General Meeting of National Provincial Bank Limited will be held on February 14 in London.

The following is an extract from the circulated statement of the Chairman (The Right Hon. The Earl of Selborne, P.C., C.H.):—

The net profit for the year is £1,460,765. This compares with £1,454,811 for 1950. The amount brought forward from 1950 is £984,462 which, added to this year's profit, gives a disposable figure of £2,454,227. An interim dividend of 7½ per cent. has been paid, accounting for £373,252. It is proposed to deal with the balance as follows:—To pay a final dividend of 7½ per cent., £373,252; to make an appropriation to Contingencies of £750,000; thereafter a balance of £957,723 will remain to be carried forward.

TRANSFORMATION IN FINANCIAL ATMOSPHERE

The past few weeks have seen a transformation in the financial atmosphere. The new Government had at once to face many pressing problems. The orgy of expenditure, in which the previous Government had indulged since the war, was bringing its inevitable retribution. How serious the situation was has been revealed in the latest announcement of the gold and dollar reserves of the sterling area. No doubt there are some exceptional factors involved in the current drain on the reserves—but the fundamental difficulty is that not only we, but other countries of the sterling area, are spending more than we are earning. In no circumstances must matters be allowed to drift and it is greatly to be hoped that vigorous measures will be taken to remedy the drain on our common resources.

The ill effects of six years of extravagance cannot be repaired in a few months, but the Government has given evidence of its determination to put a stop to inflation, which was clearly its first duty. Inflation may be unavoidable in time of war or under the stress of rapid rearmament, but in times of peace it is inexcusable. It is a primary duty of the Government of every civilised country to maintain a stable currency.

NEED FOR ECONOMIES AND REDUCED TAXATION

The control of bank credit and capital investment are merely the mechanical devices for managing the flow of money; inflation can only be stopped if the underlying pressures can also be controlled. In particular, the Government must limit the demands on our resources made by it and by the nationalised industries for which it is responsible. It is not in the national interest that private industry and trade should bear the whole brunt of the restriction of credit and higher charges. We cannot have a system of tight credit and high rates for industry and laxity in expenditure and cheap money for public undertakings. The inflation from which we are suffering cannot be cured without a heavy cut in public expenditure and a reduction in taxation. Cuts in expenditure are never easy to make, or popular, but some cuts are essential if taxation is not actually to be increased to meet the increasing cost of the rearmament programme; still heavier cuts must be devised if taxation is to be reduced. And a reduction in the present level of taxation is imperative. The cumulative effects of our taxes to-day, at their level and by their incidence, are to destroy incentive, encourage extravagance, restrict efficiency and penalise skill. They are undermining the foundations of our economy and crippling London's capacity to maintain itself as the money market of the world.

The plain fact is that the present level of national and local taxation is causing a steady erosion of personal, industrial and national assets. If, therefore, this country is to regain its economic health and increase its productivity, there must be a drastic reduction of taxation and a reform of its incidence. But the Budget has to be balanced if we are not to have a runaway inflation. In order to lower taxation, therefore, Government expenditure must be reduced. Economies are always unpleasant, but it will be more unpleasant if we are left without the means to buy food and raw materials from abroad.

INCREASED PRODUCTIVITY ESSENTIAL

In conclusion, I welcome the initial steps the Government has taken to restore confidence abroad in our solvency. We must honour our obligations, even if it involves some reduction in our standard of living. It is the only way to re-establish our credit in the world.

There remains the greatest problem of all—the question of wages, prices and cost of living. These are all chasing one another, and until the vicious spiral is broken the prospects of a recovery must be regarded as doubtful. Unless costs can be kept down, we cannot hope to sell our goods abroad in the face of competition, and with the re-entry of Germany and Japan into world markets, competition is bound to increase. In this matter, as in others, both Labour and Management must recognise that half a loaf is better than no bread, and their fullest co-operation in the spirit of partnership is more than ever necessary.

If we are to maintain our export markets we must get back to a stable monetary system and be able once again to quote firm and competitive prices. Without an increase of productivity and export there is no hope of maintaining either our present standard of life or our position in the world.

WESTMINSTER BANK LIMITED

THE NATION'S TASK

LORD ALDENHAM'S STATEMENT

THE statement by the Rt. Hon. Lord Aldenham, Chairman of Westminster Bank Limited, has been circulated to shareholders, with the Report and Accounts for the year ended December 31, 1951, which will be presented at the Annual General Meeting at the Head Office on Wednesday, February 13. The following is a summary of the statement:

Lord Aldenham, after recounting the year's changes in the Directorate, commented on the accounts. The Profit and Loss Account showed a profit of £1,405,453, a decrease of £65,578 compared with 1950. Operating expenses, mainly Staff costs, had continued to rise, but earnings had risen also; and the Bank should have been able to show an increased profit, in spite of increased taxation, but for the most unwelcome fall in the prices of British Government securities, which persisted throughout the year and, in the later months, became accentuated. This fall in British Government securities necessitated also a large encroachment upon the Bank's internal reserves.

RISE IN ADVANCES

A notable feature of the 1951 Balance Sheet was a rise of nearly £54 million in the item "Advances to Customers and Other Accounts", but a large proportion of this increase was due to borrowings by Public Authorities. Advances to industry and trade would have been appreciably larger had it not been for the Bank's compliance with the official policy of restraint upon lending.

In November, H.M. Treasury decided to fund £1,000 million of Treasury Bills by an issue of an equivalent amount of Serial Funding Loan Stock. By this means the Treasury had brought about a severe curtailment in the capacity of the banks to make further advances, and many would-be borrowers would find that it would be even harder for them to obtain from the Bank financial assistance which they might well consider to be merited.

DETERIORATION OF NATIONAL AFFAIRS

The Chairman's statement then proceeds to remark on the country's economic position in terms which may be summarised as follows:

The deterioration in our national affairs which the year 1951 has brought about is very much in all our minds. The Prime Minister told us in November that on the then existing trends and policies the United Kingdom would have in 1952 a deficit on its general balance of payments of between £500 million and £600 million, while the loss to the central gold and dollar reserve of the sterling area might be appreciably more. How gravely different a picture this gives compared with 1950, when the balance of payments for the United Kingdom showed a surplus of £221 million, and the sterling area as a whole earned a gold and dollar surplus of £287 million, exclusive of Marshall Aid.

The new Government has already taken two very important steps towards meeting our dangerous situation in making drastic cuts in our imports and in restricting credit for non-essential purposes. But it cannot even be hoped that these steps will be sufficient by themselves, and we have been warned by the Prime Minister of the need for further unpleasant action which the Government will have to take early this year.

It is greatly to be hoped that during 1952 we shall give up any complacency induced by the expression "the terms of trade have moved against us"—as if that were an adequate excuse for failure to balance our external accounts. No business could survive for long that attempted to explain losses year after year by the fact that the terms of trade had moved against it; it would have to examine its buying and its selling methods, and above all its costs, and by economy or by increased productivity bring its accounts into balance. The nation must do the same. We have done much of which we may be proud in the way of increasing the volume of our exports since the war, but not yet enough.

In almost every month from January to November the cost of living has gone up, and weekly wage rates have gone up more or less similarly. The increases in wages themselves cause further rises in prices, and rising prices lead to continuous and successful pressure for higher wages; and that pressure cannot fairly be resisted by any one industry alone.

Every increase in earnings, when not matched by increased production, lowers the purchasing power of the pound sterling and ultimately places a strain on its value in the foreign exchange market—and this at a time when all our efforts should be devoted to stabilising the value of our currency at home and abroad.

NEED FOR INCREASED PRODUCTION

The solution of most of our economic problems lies ultimately in an increase of production, and since we already have a condition

of full employment, we must secure an even greater output from our present labour force. We ought to be able to learn something from the country whose industrial output has been sufficient not only to support a high standard of living, but also to permit assistance on a most generous scale to ourselves and to other countries. The reports of the teams which have been visiting the United States under the auspices of the Anglo-American Productivity Council are well worth our study.

There has been a most welcome increase of six million tons in the total output of coal in 1951 compared with 1950, and the highest estimate of output given in the Economic Survey has been surpassed. But when we consider the improvement in the economic affairs of our own country and of all Western Europe which could be brought about by an extra 20 million tons of British coal, we see the matter in a truer perspective.

The need to defend the present exchange value of the pound sterling is very clear, and in this respect a special responsibility rests with the United Kingdom in view of her position as banker to the sterling area. The remedial measures already adopted by the Government and the foreshadowing of others to follow may be taken as a token of our determination to defend the value of the pound and to restore its prestige throughout the world.

A MAJOR PROBLEM

The need to preserve the internal purchasing power of our currency is scarcely less urgent. The question of how to check the constant tendency for prices to rise, which seems inherent in the condition of full employment, is one of the major problems of our times, and one which by no means concerns this country alone. Over a period of rapidly rising prices, coupled with our existing level of taxation, the difficulty of even replacing worn-out machines must become acute, when we ought, in fact, not only to be replacing, but to be greatly increasing, the machinery and plant serving each man at work. Moreover, a real injustice is inflicted on all individuals whose incomes are fixed; and the rise in prices is a factor which is constantly in our minds in the Bank in trying to hold the balance fairly between our Staff salaries and our earning powers.

The effect of falls in the purchasing power of money upon savings is particularly harmful. Unless the present Government's efforts to stabilise the pound are successful both the large and the small saver will see the purchasing power of their savings again decrease. Yet we all know that more and more savings are required both to reduce the pressure on consumer goods and to provide more modern and more efficient machinery for our industries.

IMPORTANCE OF THRIFT

There is an ingrained habit of thrift among the British people which could do much to check the immediate evils of inflation if it were again encouraged, or were not at least actively discouraged by the instability of the currency as in recent years. The net additions year by year to National Savings have dwindled from £444 million in 1946 to the tiny figure of £3½ million (after allowing for repayment of Defence Bonds) in 1951, and we shall have lost a most valuable weapon against inflation if this trend is not soon reversed.

We might therefore do well to alter our national attitude towards the man who saves. It is true that there are many posters exhorting him to save, but besides the loss of purchasing power of savings through inflation there are other obstacles in his way. There is little inducement for a rich man to save or even to refrain from spending his capital. If he does either, his net income is hardly affected; and as much as 80 per cent. of his capital may go in death duties. As for those persons of moderate means who help by saving out of hard-earned income, it might well suit the nation to respond to their efforts by further increasing the number of tax-free National Savings Certificates that they are allowed to hold.

FLEXIBLE BANK RATE WELCOMED

We cannot but welcome the return to a flexible Bank Rate as a measure against inflation. British banking may justly claim that the technique of the Bank Rate was first evolved in this country; but this essential part of the mechanism of credit control has for too long remained idle. Whatever justification there may have been for not using the Bank Rate in circumstances in which the need was to stimulate demand, there can be none at present when the need is, on the contrary, to damp down excessive demand. There can be little doubt that an important part of the influence of a change in the Bank Rate was always psychological. A rise in the Bank Rate was formerly accepted by the business world as a sign that a contraction of credit was needed and was imminent, and the business world quickly responded. The recent return to a policy of a flexible Bank Rate has been accepted as such a sign, and has proved, with the other measures taken at the same time, more significant than the actual rise in the rate.

As individuals we have long known that a comfortable life can be had (for a while) by living on borrowed money and neglecting our house repairs, and that it is very uncomfortable when these makeshifts come to an end. As a nation we have now reached the uncomfortable stage when we have to begin to repay the borrowings and to repair our insufficient defences. But if it were possible during 1952 for the Government and the employers and the Trade Unions, working together, to get it across to our whole nation that there is no heaven-ordained standard of living for the British people, and that it is only by our own efforts that we can surmount the difficulties with which we are at present surrounded, I should feel great confidence that the grisly spectre of idleness and hunger, so rightly raised as a warning by the Chancellor of the Exchequer, had been for ever laid.

MARTINS BANK LIMITED

MEASURES TOWARDS RESTORING SOUND ECONOMY

STATEMENT OF MR. A. HAROLD BIBBY, D.S.O., D.L.

THE one hundred and twenty-first Annual General Meeting of members of Martins Bank Limited will be held at Head Office, Liverpool, on February 12. In his statement, circulated to members, the Chairman, Mr. A. Harold Bibby, D.S.O., D.L., writes :—

First may I deal with the balance sheet and accounts which include the figures of the absorbed British Mutual Bank Limited ; I feel sure that the shareholders, in the light of existing conditions, will express their satisfaction as do my colleagues on the Board.

The net profit for the year is £725,107 which compares with £732,895 last year. The result reflects larger demands for taxation, higher overheads (the peak of which has not yet been reached), and prudent reservations facing as we now do conditions under which industry will find it less easy to make profits and the no less important changing values in British Government securities. Fortunately, an investment reserve built up in past years has, with allocations out of the year's profits, enabled the carry forward of a surplus in that particular reserve.

After payment of the dividend, it is proposed to make an allocation of £375,000 to Reserve for contingencies.

Total assets amount to £347,336,244 against £342,053,859.

Customers' funds and other accounts are £314,582,055 against £303,348,987 last year and advances are £88,603,419 as compared with £74,809,980.

Changes in other assets will be observed in the comparative balance sheet ; the ratio to deposits of our more liquid resources, including Treasury Deposit Receipts stands at 35.73% ; the fall from the high figure of a year ago is accounted for mainly by the translation of £24,000,000 of Treasury Bills into the new 1¾% Serial Funding Stocks, being a reflection of the Government's early steps towards monetary stability.

CHANGES IN DIRECTORATE

The past year has again seen changes in the Directorate of the bank and in the Local Boards. I have to record with deep sorrow that Sir William Clare Lees, Bart., O.B.E., LL.D., passed away in May. He had rendered great service to the bank during the eighteen years of his close association, first as a member of the Manchester Board where he had served as chairman for over nine years, and later as a member of the General Board where he acted as a deputy chairman from 1945 onwards.

During the year we welcomed to our deliberations Sir Wilfrid Martineau, M.C., T.D., M.A., a partner in the firm of Messrs. Ryland, Martineau & Company, Solicitors, of Birmingham. We are indeed fortunate in having his co-operation both on the General Board and also as chairman of the newly constituted Midland District Board to which I refer later. Mr. P. J. D. Toosey, D.S.O., O.B.E., T.D., who has wide commercial interests in the North West has, I am pleased to say, also joined the General Board.

Mr. Myles N. Kenyon, D.L., whose valued counsel has been available for many years both to the General and Manchester Boards, has been elected as chairman of the Manchester Board, and Mr. R. Cary Reynolds, O.B.E., has joined that Board. From the North Eastern Board Sir John S. Barwick, Bart., has retired owing to advancing years and we record our appreciation of the services he rendered over the long period of 35 years. To fill the vacancy Mr. Peter Wrightson, O.B.E., has accepted a seat on that Board. In Mr. Reynolds and Mr. Wrightson we have colleagues with wide knowledge and experience in their respective spheres of textiles and engineering whose advice will be invaluable.

In May last Mr. Herbert Holt relinquished his seat on the Leeds Board to which he was appointed in 1941 following notable service in an executive capacity. His total service with the bank and its predecessor extended over sixty years and we acknowledge his valued co-operation.

EXTENSION OF DECENTRALISATION

Once again may I stress the advantages which accrue both to the bank and customers generally in our policy of decentralisation through our Local Boards and District Head Offices. During the year we have put into effect a further extension of this system for it was decided that the growth and control of our business in the Midlands would be greatly facilitated by establishing a Local Board with district general management at Birmingham : this new arrangement will prove, I am sure, a considerable source of strength to our organisation. As I have already mentioned we are fortunate in securing the services of Sir Wilfrid Martineau on the General Board, and he it is who will be the first chairman of the Midland District Board. He is a prominent figure in the

civic life of Birmingham and has filled the high office of Lord Mayor ; his counsel and his breadth of knowledge of that area will be of great help as also will the assistance of Mr. P. H. Jones, M.C., T.D., D.L., M.I.Mech.E., a well-known Midlands industrialist who has joined him as a member of the Midland District Board.

PROMOTING OVERSEAS RELATIONS

Mr. C. J. Verity, chief general manager, made an extensive tour of Australia and New Zealand during part of last year making numerous calls on Australasian banks and commercial houses, and I know that his visit has been of real value in cementing and promoting business relations with that steadily growing continent. Other executive officers have also visited and kept in touch with our connections abroad.

You will remember that a while ago in order to meet our expanding needs for office accommodation, we acquired premises at 80 Gracechurch Street, London. I am now able to tell you that after much frustration in the process completion of the alterations there is imminent, and our Chief Foreign Branch, the London Trustee Department and some other internal departments are to be housed in these premises (to the relief of space at 68 Lombard Street) and in addition we are opening a new branch there.

Amongst several new branches opened during the year it is notable to record that an office is now functioning in St. Helier, Jersey, and a subsidiary company to meet local regulations has been formed for the purpose of carrying on trustee business there.

Before leaving the domestic sphere it is appropriate that I should make reference to the valuable service rendered by the staff and reflected in the annual report. The results are witness to the untiring efforts and constant attention of the chief general manager and his deputy, his colleagues of the general management, the district general management and branch managers, and also to the zeal and efficiency of the staff as a whole, for which we offer them our sincere thanks and appreciation.

The past year has been difficult for everyone and not the least for bankers. All the uncertainties of a troubled world, the precarious and unstable foundations of our domestic economy, the financing of stocks at high prices, the difficulty of obtaining risk capital, have added to the perplexities of the problems with which bankers are called upon to deal.

However, beyond trying to profit from the lessons, there is little merit in dwelling on the difficulties in too much detail when one's thoughts and energies should be directed to the future rather than to a post-mortem on the past.

CREDIT TO BE USED TO NATIONAL ADVANTAGE

The Government have announced their programme to curb inflation by the restriction of credit and, as an aid to this, by higher interest rates.

MARTINS BANK
LIMITED

STATEMENT OF ACCOUNTS, 31st December, 1951

LIABILITIES

Capital paid up	£4,315,096
Reserve Funds	4,705,821
Current, deposit and other accounts (including Profit and Loss Account)	314,985,008
Acceptances and engagements on account of customers	23,330,319
	£347,336,244

ASSETS

Cash in hand and at Bank of England	£26,455,079
Balances with, and cheques in course of collection on other banks in the British Isles	16,772,988
Money at call and at short notice	47,018,250
Balances with banks abroad	658,403
Treasury Bills	29,665,000
Treasury Deposit Receipts	4,000,000
Bills discounted	5,401,791
Investments	101,171,693
Advances to customers and other accounts	88,603,419
Trade Investments	446,399
Bank Premises	3,812,903
Liability of customers for acceptances and engagements	23,330,319
	£347,336,244

LONDON DISTRICT OFFICE : 68 LOMBARD STREET, E.C.3.

HEAD OFFICE : WATER STREET, LIVERPOOL, 2

Bankers are asked to examine most carefully all applications for fresh loans and the renewal of old ones. The yardstick will be whether the money is required for projects which are essentially and positively related to the re-armament programme, to the stimulation of exports to desirable markets, to the saving of imports, particularly from dollar sources, and to the relief of basic deficiencies, especially of raw materials ; if these tests are not passed the banks are asked to be much more restrictive however credit-worthy the applicant may be.

The truth is that credit is in short supply and it is only by using the amount available to the best national advantage that the essential business of the country can be kept running. To achieve this there may have to be some re-orientation of trade, but it is not proposed that there should be disorganisation of trade by the sudden withdrawal of banking facilities: it must be recognised however that everyone will have to reduce their credit requirements to the minimum and not embark on unessential expansion.

The home consumption trades will suffer most and no doubt the hire purchase business, which runs from Rolls Royce cars to electric kettles, will be among these. Government-owned industries, like gas and electricity, are among the most prominent promoters of hire purchase and the reaction in these nationalised businesses will be a sound indication of the pressure the Government wish applied.

It is to be hoped that whole-hearted support will be forthcoming from every industry and every individual in this strenuous attempt to deal with a situation which might well cripple our whole economy.

MAXIMUM INDIVIDUAL EFFORT NEEDED

Ever rising costs are the nightmare which to-day haunts everyone. This problem presents itself to each individual in a different way ; to the industrialist it is the increasing cost of raw materials and wages making his product too dear ; to the widow it is the rising cost of the food and clothing to maintain existence at all ; to the nation it is being able to sell abroad our exports to pay for the food and raw materials we must import if employment and the necessities of life are to be available to us.

The one factor common to everyone is just that the £ has ceased to purchase what it formerly did. On this subject so much has been said and written both by the learned and the ignorant that the ordinary man in the street becomes utterly confused and bewildered and he clings to the fixed though mistaken belief that if he is to maintain anything approaching his present standard of living he must have higher wages or a higher margin of profit (whichever applies to his particular case).

The general bewilderment obscures what is surely the fundamental fact, namely, if each and all expect to receive £1 for 10s. worth of work or goods it cannot be long before the £ generally becomes worth only 10s.

So long as this present day attitude continues, the purchasing price of the £ must decline and the only way to arrest the trend and make the purchasing price of the £ increase is to give something of more value than £1 for the £1 reward which we demand for our individual effort, be it of brain or muscle.

Rearmament, which we all agree is necessary for our very existence, must absorb a large portion of that extra effort and it is only what we are willing and ready to give over and above the rearmament requisite that is going to make our earnings worth more.

We all pay lip service to the need for higher production but most of us think that that is a matter for the other man and has little concern with ourselves. Till each and everyone of us is determined and resolute to give the maximum of his or her effort each day and every day, no fall in the cost of living or appreciation in the real value of the £ can possibly take place.

We, in this generation, are having to pay the cost of winning two world wars and trying to prevent a third and that can only be done by giving in effort something over and above our living requirements. No section of the community can or should expect to be shielded from this.

The choice is quite clear—either to contribute a higher degree of effort or to accept without complaint a lower standard of living.

REARMAMENT'S PRIOR CLAIM ON EARNINGS

Without falsifying reality it is only possible to spend £1 once. This is equally true in the national as in the individual sense. If this is accepted, the question is " How much is there in the national purse and how can it best be spent ? "

To use a business simile, the position can be compared with the rights or claims of three types of capital in a big industrial company.

Debenture interest has priority of charge against income and then preference shares and ordinary shares get their rewards in that order. The vast majority of people have come reluctantly to the conclusion that for the safety of our country, our homes, our families and our way of life, rearmament must, like debenture interest, have priority of charge upon the income of our national community ; the rewards for the preference shares must go to maintenance and improvement of our present equipment and the provision of new. This only leaves the rewards of the equity, that is, the surplus of income left after meeting all prior claims, to provide for private and public spending ; in other words this surplus is reflected in our standard of living, individually by our private spending in normal living expenses and in those extras such as a television set or a seaside holiday, and collectively

through the taxes paid, by the community at large, used either by the local or national authorities on the maintenance of roads, hospitals, education and other social amenities.

Having met the fixed debenture and preference charges, the sum we can spend on the rest depends entirely on what surplus, if any, there is for the ordinary shareholders who are in this allegory the public at large. We all know that this depends on the prosperity of the concern as a whole.

Under careful and wise management with everyone pulling his full weight, with incentives to do so, there should be good dividends for the ordinary shareholder but, given extravagant, inefficient management at the top and slack disinterested workmanship below there can be little or nothing for the holder of the ordinary shares except, perhaps, during a short-lived international sellers' market.

SOCIAL SECURITY AND WELFARE STATE MUST BE WORKED FOR

Social security and the welfare state which depend on the dividends from the ordinary shares are, therefore, not things that like manna drop from heaven, but have to be worked for here on earth.

Unless this is fully appreciated, the whole idea of social security is false and misleading and tends to an unreal sense of well-being which breeds indolence and lack of any sense of drive and sustained effort.

Would we not be wiser to build up our collective security on a foundation of individual security ?

Each one of us, by striving to become a master of his profession, craft or trade, by refusing to be content with the second rate or shoddy, be it at the desk, the bench or in the field, would recapture a sense of individual self-reliance and a pride and happiness in our diversified occupations. With encouragement and reward for good honest work, sloth and dodging the column would disappear.

It could be argued that this was all very well for the able-minded and able-bodied and that the weak, aged and feeble would be driven to the wall. In these enlightened days no one is, or should be, allowed to fall below a reasonable standard ; society from the top to the bottom would revolt against any individual or section of the community living, by no fault of their own, below decent standards of life.

Given that surge forward in effort, that striving and pride in doing a job well, the dividends for what in my simile I have called the ordinary shareholders would rise to such heights as to provide comfort for the old and sick and added incentive to the adventurous, hard-working and self-reliant.

PROFICIENCY BONUSES AS INCENTIVES

Everyone agrees consciously or unconsciously that incentives are good ; even the most hard-boiled trade unionist of the old school concurs or, if he has any doubts, his wife certainly hasn't.

From infancy we have been brought up on incentives and rewards ; the small child is offered a sweet ; the school child is offered a prize ; in sport it is universal. In fact, after centuries of trial and error, it emerges as the logical and best method of urging humans to give of their best.

There are many ways of offering incentives, the difficulty is in selecting the best.

At first sight, profit-sharing seems the easiest and fairest way, but this may defeat its own object.

First of all, it presumes that there are profits to share but, supposing there are when the scheme is inaugurated and that they continue for a number of years, then the happy recipients in the first year or so accept the bonus as something over and above the standard wage but, very soon, it is regarded as a regular part of their remuneration and is absorbed into a revised standard of living, be it a larger house, a better school for the children, or any of the things we all hope and strive for.

Sooner or later the cycle of trade results in lower profits, or in no profits at all. If there is a loss, those who participated in the profits are economically unable to share in the loss. However, if the bonus disappears, or is even diminished, then unless it has been regarded entirely as savings, which is rare, financial hardship at once confronts the family and the feeling of encouragement that the scheme first produced is turned into one of frustration and insolvency.

To avoid this, bonuses could be invested in the individual names of employees in some form of Government stock, or in the business itself, in such a way that they could not be cashed for current expenditure but the interest paid half-yearly to the holder. This has the disadvantage that a £1 a week bonus becomes an uncashable saving of £52 per annum, with an interest payment of only £2 to £3 a year before deduction of tax. Human nature being what it is nearly all the incentive would disappear. Is there any other method that avoids these two disadvantages and is direct and sufficiently immediate ?

With the co-operation of the trade unions who, in general, accept the principle of incentives in piece-work and differentials, a comparatively simple scheme of proficiency bonuses could be given individually and, among the clerical staffs the inducement to give a full best could be with the emphasis on proficiency rather than on a graded basis of age or years of service.

These bonuses, though smaller than profit-sharing in boom times, would be permanent so long as they were merited by the efficiency of the individuals concerned and would be divorced from trade cycles and other matters beyond the employees' control.

I believe some such scheme, which would differ from business to business, would meet the aspirations of those who wished to better their circumstances by their own endeavours—that, surely, is the essence of incentives.

DISTRICT BANK LIMITED

HIGHLY SATISFACTORY TRADING RESULTS

INTENSIFICATION OF ECONOMIC DIFFICULTIES

UNIFIED PLAN OF CAMPAIGN TO COMBAT INFLATION

SIR THOMAS D. BARLOW ON NEED FOR SACRIFICES

THE Chairman, Sir Thomas D. Barlow, C.B.E., has circulated with the report and accounts his statement to the shareholders of District Bank Ltd., prior to the 122nd annual general meeting to be held on February 8 at the head office, Spring Gardens, Manchester.

In the course of his statement the Chairman said:—

Compared with a year ago the Balance Sheet shows variations, which, to some extent, have been brought about by the monetary measures taken by the Government in the autumn. Our deposits show only a small variation and stand at £238,000,000. Cash and money at call and short notice have increased by £3,000,000, but, largely as a result of the Government's funding of a substantial part of the Floating Debt last November our holdings of Treasury Bills are reduced and figure at £31,000,000. Notwithstanding this change our liquid position remains satisfactory.

Following the change in monetary policy there has been a decline in the value of gilt-edged securities. We have not escaped some measure of depreciation, but our inner reserves are well able to take care of the position and, as hitherto, the investments appear in the balance sheet at less than their market value.

Last year our advances increased by over £8,000,000. These additional facilities were required chiefly by customers engaged in exports or other work of urgent national importance. The rise in prices of raw materials, heavy taxation and the increased wages paid in industry largely explain the growing demand for accommodation. In the course of this year it is more than likely that we shall be called upon for further assistance, especially from those engaged in all the ramifications of the rearmament programme.

One way or another there is no doubt about industry's needs for temporary finance. As there is also an overriding injunction to restrain bank lendings for the non-essential industries so as to combat inflation, our duty as bankers is plain, but this does not make the execution of our task any easier. By increasing the bank rate and at the same time calling upon the banks "to continue and intensify their efforts to restrict credit to essential purposes" the Chancellor wishes it to be understood that requests for advances will be more critically examined. In what we are called upon to do no drastic deflation is contemplated. On the contrary we are to exert an influence in support of a gradual disinflationary policy. It is, of course, impossible to know exactly how tight banking restraint upon lendings will have to be. That will be effectively determined by the Treasury through its control over the cash and liquid resources made available to the banks—the credit-base itself. In the meantime our task of interpreting official policy will be made less difficult if customers will not seek accommodation without first carefully considering the validity of the purpose for which it is required. I should also like to point out that a curtailment of an important function of banking, prudent lending, is not conducive to increasing our earnings. If those who look to us for financial assistance will only appreciate this aspect, they will more readily understand that now, as in the past, it is because of urgent and important Government directives that we have to refuse credit-worthy applications which we would have no hesitation in sanctioning in normal times.

THE YEAR'S PROFIT

The net profit for the year amounts to £508,217 and compares with £513,168 for 1950. With the amount brought in from that year there is for disposal £790,001. We have allocated £225,000 to reserve for contingencies. After this deduction, and allowing for dividend payments at the same rate as formerly, there remains a sum of £301,345 to be carried forward. The results, I think you will agree, are highly satisfactory, bearing in mind the increase in running costs and the higher rates of taxation which industry in general continues to experience.

THE ECONOMIC SITUATION

The economic difficulties accumulating in this country over the last few years have now been intensified by the rearmament programme. As a consequence we are confronted with a dollar deficit when the re-payment of the previous dollar loans has begun and when foreign competition, together with the import and credit restrictions imposed by other countries, is interfering with the sale of our goods abroad. This situation is, of course, partly responsible for the present gap in our balance of payments, but, as with previous deficits, our real weakness lies in the fact that we have so persistently failed to adjust the country's internal economy to the limits of

what it can afford. Instead, we have continued physical controls and penal taxation and resorted to devaluation and to the running down of stocks of raw materials and food. The inadequacy of these measures having at length been proved we are this time attempting more far-reaching correctives and they must be applied vigorously, however unpleasant the process may be.

With home consumption, investment and defence monopolising so much of our industrial resources the amount available for exports is hardly sufficient to pay for even indispensable imports. The chief cause of the trouble is still excessive internal expenditure. The deficit in our external trade is now, as in the past, but a symptom of our domestic inflation.

This can no longer be ascribed entirely to the war or immediate post-war periods. Devaluation and the conflict in Korea greatly increased the cost of our imports, as did belated purchases of these in 1951. The effects, having worked their way through productive and distributive costs, have brought in their train demands for increased wages. With wages chasing prices at a time when defence expenditure is mounting, the country is in danger of a worse phase of inflation and one which, expressed in terms of increasing demand, can only lead to most critical shortages of both materials and labour, thereby retarding essential production at the very time it should be greatly increased. If we are to prevent such a serious situation it is clear that inflation is the first evil to subdue. This will be no easy battle, since it has to be fought on many fronts, but is much more likely to be won now that the forces marshalled against it have been strengthened and concentrated in a unified plan of campaign.

THE BROADER ISSUES

It remains to be seen how long it will take orthodox monetary control, with all possible economy in administration and in private and public expenditure, to halt the inflationary spiral and restore our national prosperity. Past experience has shown that we have been able to count on the utmost endeavour when our national needs are most pressing. Nevertheless the sacrifices which these emergency measures entail will be felt by all sections of the community in varying degree and it would be idle to pretend that the general experience will not be both painful and severe.

A constant factor which runs through all historical experience is that the creation and accumulation of capital are essential conditions of a country's survival whatever its form of government. We may perhaps be permitted to believe that ours is the more excellent way. But if we continue to draw too freely on such reserves as we still retain, and if we are not willing to make the necessary sacrifices, it is very certain that our way of life cannot be preserved and that we can only look forward to a situation in which it will be difficult to support fifty million people and maintain their present standard of life.

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